Market Commentary Monday, January 23, 2023

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EXECUTIVE SUMMARY

Newsletter Trades – Sold a Portion of our JBL stake
Sentiment – Main Street Becomes More Optimistic
Econ Numbers – More Negative than Positive in the Latest Statistics
Econ Outlook – Little Change in the Forecast; Corporate Profits Likely to Remain Solid
Inflation – PPI Pulls Back; Modest Reduction in Market Projections for Peak Fed Funds Rate
Washington – Favorable Historical Evidence & Debt Ceiling Perspective
Wall of Worry – Plenty About Which to Fret, But Stocks Long Have Proved Resilient
Valuations – Inexpensive Metrics for our Portfolios
Stock News – Updates on JWN, GS, MS, CFG, PNC, TFC, FITB, KEY, CMA & OZK

Market Review

As discussed on Wednesday's *Sales Alert*, we sold 375 and 85 shares of **Jabil Inc.** (JBL – $79.42) respectively held in TPS Portfolio and Buckingham Portfolio on Friday, January 20, at $78.43.

We will use that price to close out the 940 and 161 shares of JBL respectively trimmed that same day in our hypothetical PruFolio and Millennium Portfolio.

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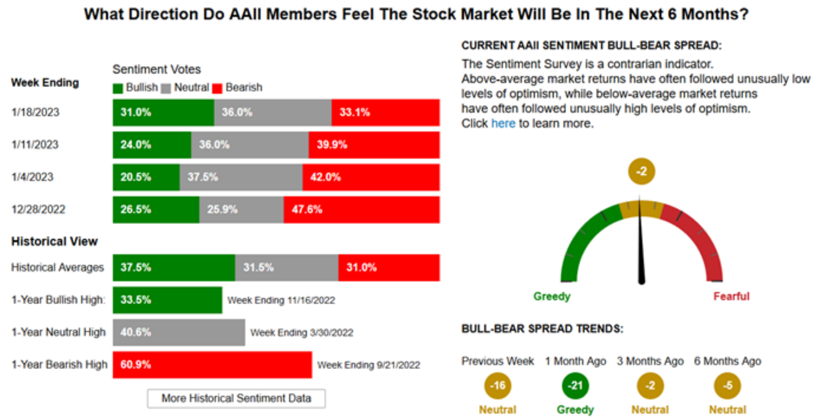
We were all set to attribute last week's sizable setback in stocks that had been shaping up as of Thursday evening to the big improvement in investor sentiment at the American Association of Individual Investors (AAII).

After all, the gauge is widely viewed with a contrarian eye, so the tally of Bulls in the latest AAII Sentiment Survey rising to 31.0% and the number of Bears falling to 33.1% has taken the measure to a much more neutral level and out of extreme pessimism territory, with the Bull-Bear Spread now residing at minus 2.1%.



AAII Bull-Bear Spread

Decile	Low Reading of the Range	High Reading of the Range	Count	R3K Next 1-Week Arithmetic Average TR	R3K Next 1-Week Geometric Average TR	R3K Next 1-Month Arithmetic Average TR	R3K Next 1-Month Geometric Average TR	R3K Next 3-Month Arithmetic Average TR	R3K Next 3-Month Geometric Average TR	R3K Next 6-Month Arithmetic Average TR	R3K Next 6-Month Geometric Average TR
	Below & Above Median Bull Bear Spread = 7.18										
BELOW	-54.0	7.2	925	0.24%	0.20%	1.14%	1.00%	3.28%	2.88%	6.47%	5.70%
ABOVE	7.2	62.9	924	0.17%	0.15%	0.53%	0.44%	2.00%	1.75%	4.63%	4.15%
	Ten Groupings of 1848 Data Points										
1	-54.0	-16.9	185	0.41%	0.34%	2.02%	1.78%	4.43%	3.90%	8.20%	6.99%
2	-16.8	-8.7	185	0.23%	0.20%	0.82%	0.67%	3.49%	3.12%	6.24%	5.45%
3	-8.6	-2.3	185	0.34%	0.30%	1.14%	1.03%	3.22%	2.80%	7.53%	6.80%
4	-2.3	2.7	185	0.15%	0.12%	1.01%	0.92%	2.50%	2.13%	5.31%	4.76%
5	2.7	7.1	184	0.06%	0.03%	0.68%	0.58%	2.71%	2.44%	5.03%	4.49%
6	7.2	11.6	185	0.20%	0.18%	0.70%	0.61%	2.00%	1.76%	4.76%	4.29%
7	11.7	16.0	185	0.12%	0.10%	0.41%	0.28%	2.44%	2.19%	5.26%	4.75%
8	16.1	21.8	185	0.15%	0.13%	0.91%	0.84%	2.26%	2.02%	5.82%	5.40%
9	21.9	29.0	185	0.15%	0.13%	0.36%	0.28%	1.83%	1.53%	4.78%	4.21%
10	29.0	62.9	185	0.23%	0.21%	0.30%	0.23%	1.51%	1.29%	2.60%	2.15%

From 07.31.87 through 01.19.23. Unannualized. SOURCE: Kovitz using data from American Association of Individual Investors and Bloomberg

The good folks in the AAII Sentiment Survey are much more optimistic today than they have been in a long while, even as they are still far more pessimistic than has been normal over the last 36 years.

To be sure, this is well below the normal level of optimism usually seen, and we still think the metric is suggesting investors should be greedy when others are fearful, but subsequent returns data generally show that the more pessimistic investors are, the better returns will be going forward.

Alas, as AAII illustrates, far too many folks zig when they should have zagged. For example, per data analytics firm DALBAR, equity fund investors had awful relative returns in 2021, gaining only 18.4% on average, compared to a 28.7% return for the S&P 500, for a whopping 1030 basis point (10.3%) difference in performance. The longer-term historical numbers are even worse for bonds as Fixed Income fund investors had an annual return 500 basis points lower than the U.S. Aggregate Bond index over the past three decades.

Individual Investor Returns vs. Broad Benchmarks							
	Stocks			Bonds			Inflation
Time Period	Average Equity Investor Return	S&P 500 Return	Difference	Average Bond Investor Return	U.S. Aggregate Bond Index Return	Difference	U.S. Consumer Price Index
1 Year	18.4%	28.7%	-10.3%	-1.6%	-1.5%	-0.1%	7.0%
3 Years	21.6%	26.1%	-4.5%	1.7%	4.8%	-3.1%	3.5%
5 Years	14.8%	18.5%	-3.7%	0.8%	3.6%	-2.8%	2.9%
10 Years	13.4%	16.6%	-3.2%	0.4%	2.9%	-2.5%	2.2%
20 Years	8.1%	9.5%	-1.4%	0.4%	4.3%	-3.9%	2.3%
30 Years	7.1%	10.7%	-3.6%	0.3%	5.3%	-5.0%	3.4%

From 12.31.1984 through 12.31.2021. Annualized returns. SOURCE: Kovitz using data from DALBAR and Bloomberg Finance L.P.

Data compiled by DALBAR show that equity (and fixed income) fund investors generally have been awful at timing their moves into and out of stocks (and bonds), with very detrimental long-term consequences.

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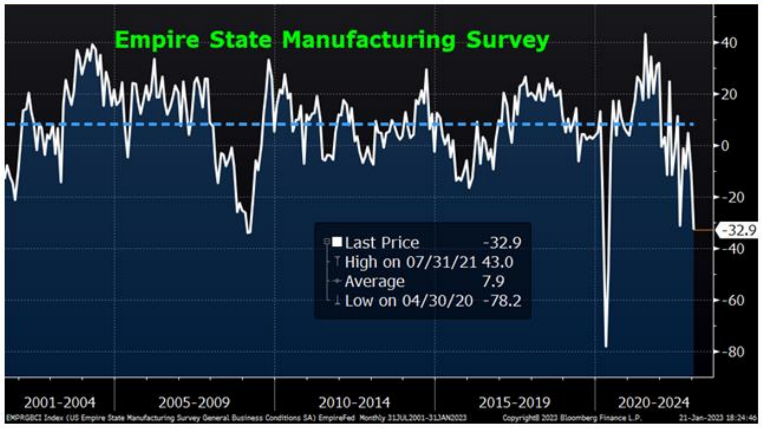
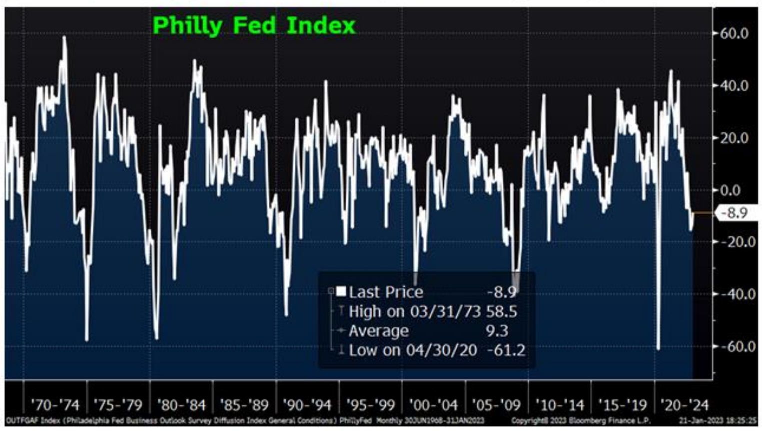
We might also have placed the blame on the latest batch of economic data, especially as *The Wall Street Journal* told us on Thursday evening, "Stocks Fall as Data Signal Slump."

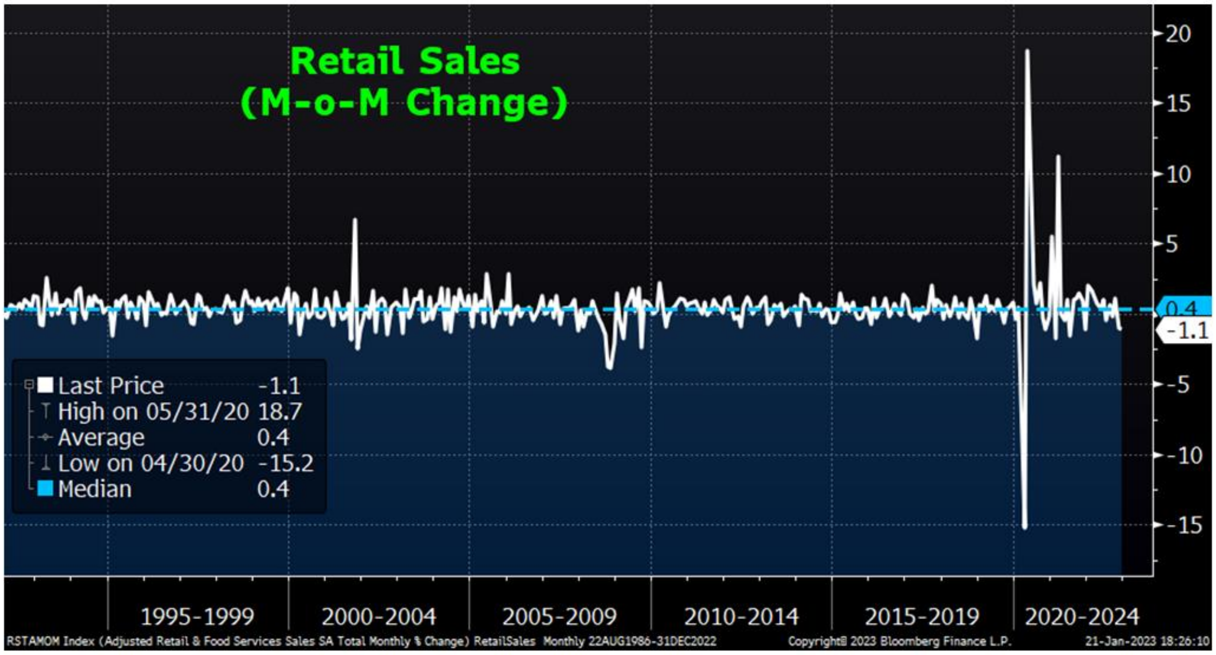
Indeed, two indexes of East Coast factory activity are in contraction and well below their norms. The Empire State gauge of manufacturing activity in the New York area weakened in January to a much-worse-than-expected minus 32.9, down from minus 11.2 in December. On the other hand, the Philadelphia Fed's measure of manufacturing activity in the mid-Atlantic region improved in January to a reading of minus 8.9, which was above forecasts even as it was down from minus 13.7 in December.





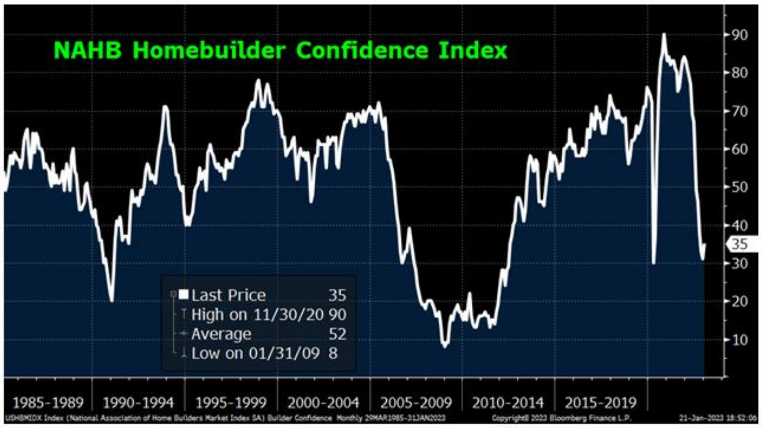
Two key manufacturing gauges are in contraction, though the Philly Fed factory index improved this month.

More importantly, with November's reading coming in at a revised 1.0% decrease, retail sales last month slipped by a seasonally adjusted 1.1%, a tad worse than estimates. Clearly, the consumer has been tightening his or her pocketbook, but total sales for all of 2022 were up 9.2% over 2021, no doubt boosted by much higher inflation.



Retail sales were strong in 2022, though the year ended on a decidedly negative note.

Turning to new home construction, the National Association of Home Builders' monthly confidence index for January beat forecasts, climbing to 35, up 4 points from December, though the figure was well below the long-term average on the 35-year-old gauge. High prices and the spike in mortgage rates did not help, and ground was broken on just 1.38 million homes last month, in line with what was reported in November. Building permits came in below expectations in December, dipping to 1.33 million units, down from 1.35 million the month prior.



Not surprisingly, given the jump in mortgage rates, new home construction has weakened considerably.

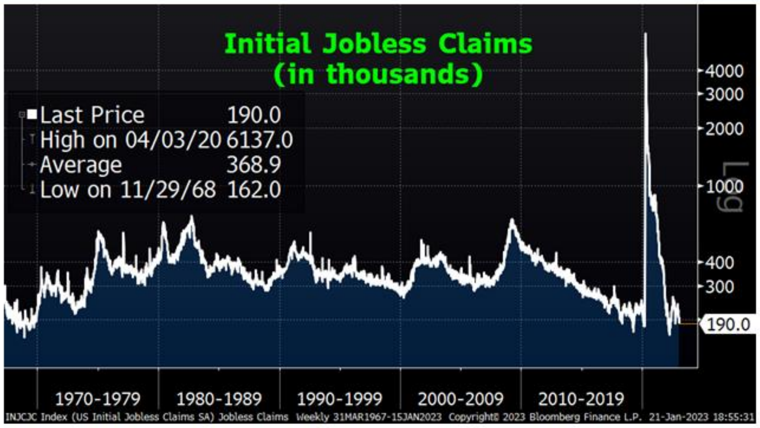
And other economic numbers were not exactly robust. U.S. existing home sales fell by 1.5% in December to a seasonally adjusted annual rate of 4.02 million, a bit better than projections but the 11th straight monthly decline as higher interest rates and elevated prices weighed heavily on affordability. Meanwhile, industrial production edged lower by 0.7% in December to 78.8%, weaker than estimates of a slight advance and falling from the November tally of 79.4%. Manufacturing output dropped 1.3% and capacity utilization of 78.8% came in below expectations.

Economic stats out last week like existing home sales and industrial production left a lot to be desired.

All that said, it isn't as if there has been much change in the economic outlook of late. The respective 1.6% and 0.6% contractions in Q1 and Q2 2022 real (inflation-adjusted) GDP means economists could say that the U.S. economy was already in recession, but the odds of an official declaration have held steady at 65.0%, even as the latest consensus forecast for GDP growth this year is 0.5% and 1.2% for 2024.

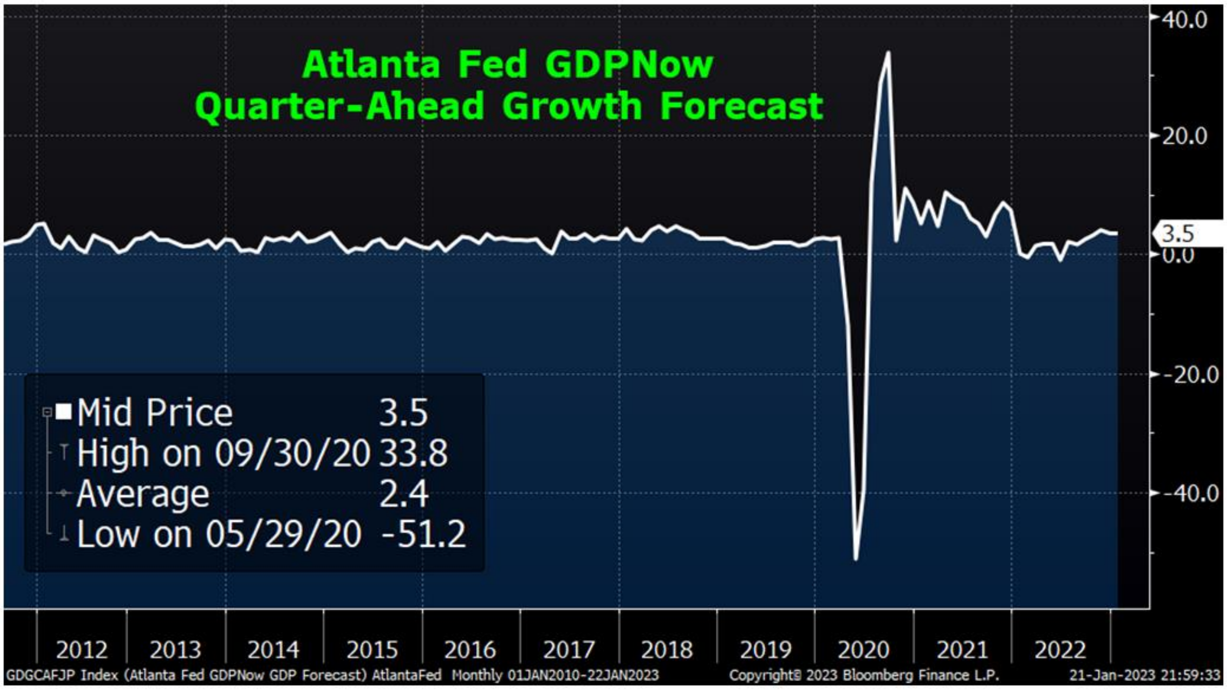
Economic forecasts are often fraught with peril, but the prognosticators now project a nearly two-thirds chance of a U.S. recession occurring in the next 12 months.

Further, the jobs picture remains very healthy. While higher than readings earlier in 2022 with a 1-handle, yet still coming in near the lowest levels since 1969 when the work force was much smaller, new filings for unemployment benefits for the period ended January 14 were a seasonally adjusted 190,000, down from a revised 205,000 the week prior. Continuing claims filed through state programs inched up to 1.65 million, as businesses continue to hold onto most workers with qualified labor difficult to obtain, though the tally is expected to move up.



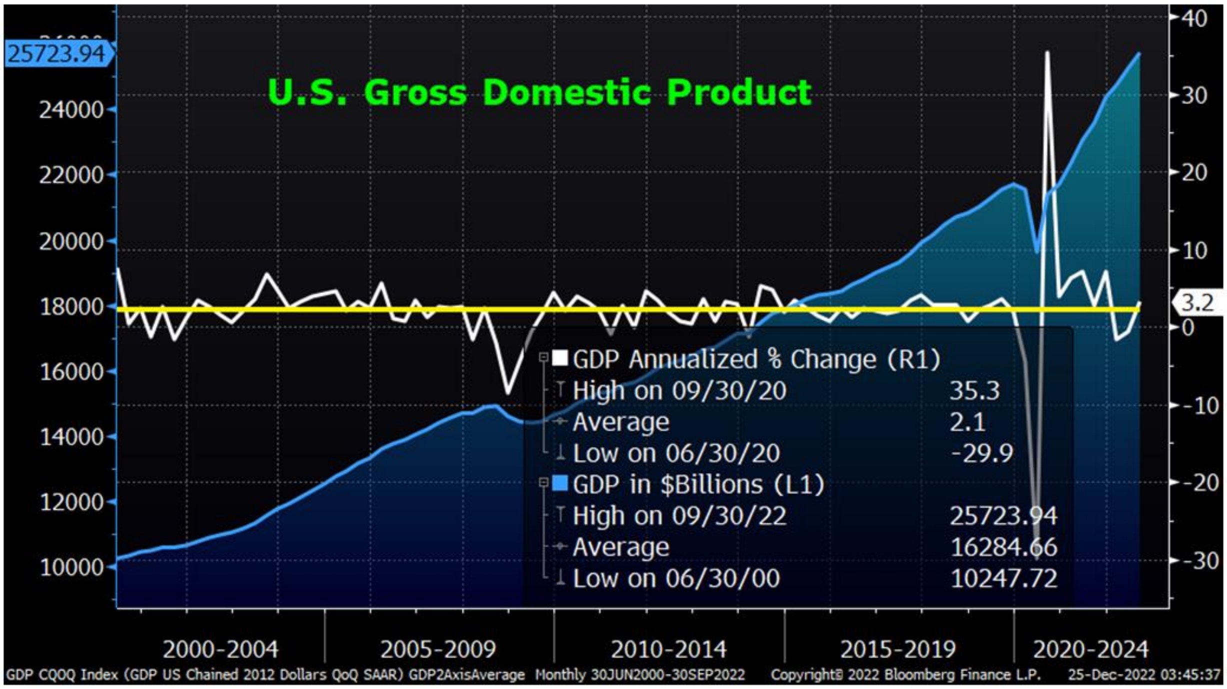
The labor market remains robust with jobless claims still near five-decade-plus lows.

Also, we can't forget that even as the Omicron variant, supply-chain difficulties, the war in Ukraine and inflation impacted the economy, domestic growth in Q3 rebounded to 3.2% and the Atlanta Fed's projection for Q4 2022 real GDP growth on an annualized basis as of January 20 stood at a strong 3.5%.



It is fascinating to see so much pessimism toward the U.S. economy when the current estimate for Q4 real (inflation-adjusted) GDP growth resides at a handsome level.

We believe, as does the analyst community, that the economy will remain healthy enough to provide a positive backdrop for corporate profits. That does not seem to be much of a stretch when we consider that third quarter 2022 current-dollar nominal GDP of $25.7 trillion soared by 9.2% on an annualized basis to an all-time high. Yes, economists always focus on real (inflation-adjusted) numbers, but sales, earnings and stock prices are always measured in nominal dollars.



There was a huge 9.2% jump in Q3 nominal GDP, even as real (inflation-adjusted) growth was “only” 3.2%.

It is still very early in the current reporting season, but Q4 EPS have been decent thus far, with 69.0% of the 55 companies in the S&P 500 to have announced results beating bottom-line expectations. Of course, outlooks have been subdued and stock prices often have reacted negatively.

S&P 500 Earnings Per Share		
Quarter Ended	Bottom Up Operating EPS 3 Month	Bottom Up Operating EPS 12 Month
ESTIMATES		
12/31/2023	$58.86	$225.35
9/30/2023	$57.87	$219.67
6/30/2023	$55.59	$212.15
3/31/2023	$53.03	$203.43
12/31/2022	$53.18	$199.76
ACTUAL		
9/30/2022	$50.35	$203.31
6/30/2022	$46.87	$204.98
3/31/2022	$49.36	$210.16
12/31/2021	$56.73	$208.21
9/30/2021	$52.02	$189.66
6/30/2021	$52.05	$175.54
3/31/2021	$47.41	$150.28
12/31/2020	$38.18	$122.37
9/30/2020	$37.90	$123.37
6/30/2020	$26.79	$125.28
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

Source: Standard & Poor's. As of 1.12.23

Certainly, we realize that analysts are often overly optimistic in their earnings outlooks, but Q4 2022 results have been solid thus far and the outlook for 2023 is still for significantly higher EPS.

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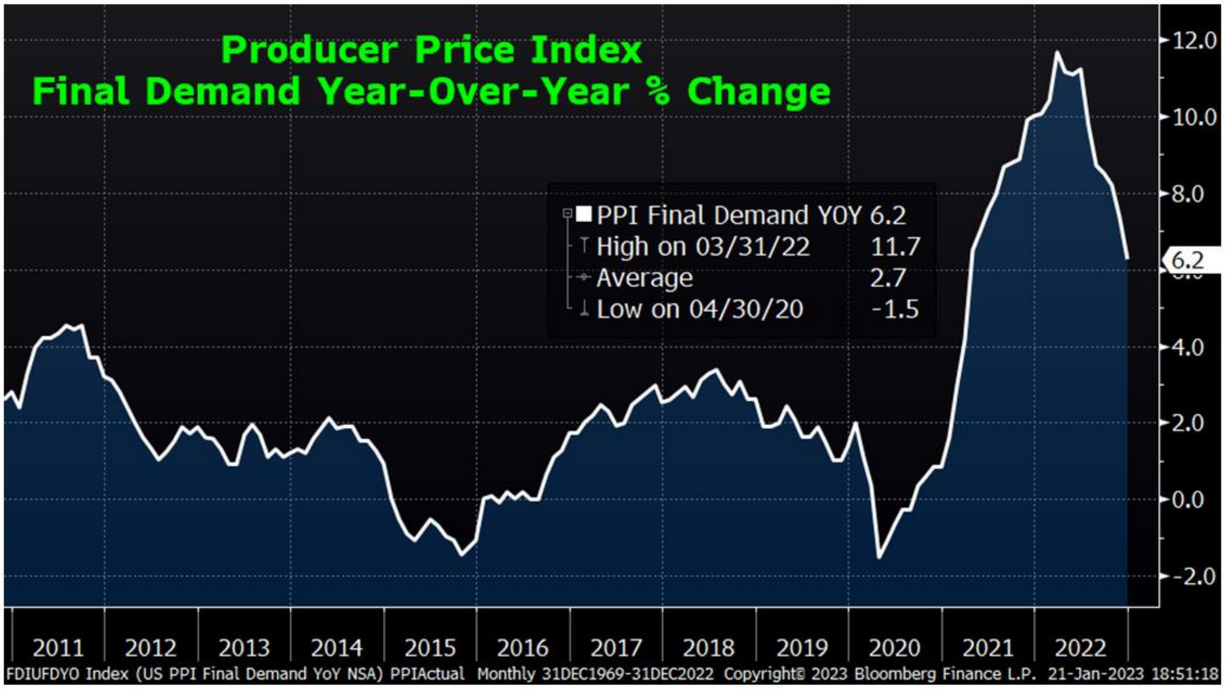
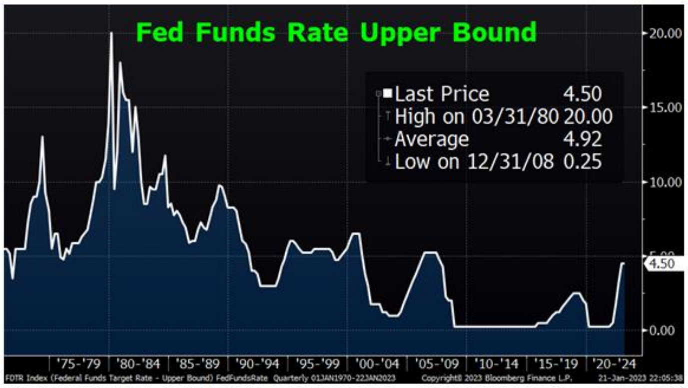
Concerns about inflation and the Federal Reserve have also been weighing on investor psyches, but the gain in wholesale prices continued to retreat in December. The producer price index dropped 0.5% last month, the largest decline since 2020, with the year-over-year rise falling to 6.2%, down from 7.3% in November and 11.7% last spring.



The year-over-year increase in inflation at the wholesale level continued to fall in December.

Although the estimate for real GDP growth in 2023 was pared to 0.5% in December, down from 1.2% in September, the Federal Reserve lifted its target for the Fed Funds rate by 50 basis points last month, following 75 basis point hikes at each of the June, July, September and November FOMC meetings. Jerome H. Powell & Co. are now projecting that the Fed Funds rate will likely end 2023 at 5.1%, but the Fed Funds futures became a bit less hawkish last week as they are now estimating a 4.42% year-end 2023 Fed Funds rate and a 4.90% peak in June 2023, with a pivot lower coming in July.



Meeting	#Hikes/Cuts	%Hike/Cut	Imp. Rate Δ	Implied Rate	A.R.M.
02/01/2023	+1.033	+103.3%	+0.258	4.589	0.250
03/22/2023	+1.805	+77.2%	+0.451	4.782	0.250
05/03/2023	+2.248	+44.3%	+0.562	4.893	0.250
06/14/2023	+2.292	+4.4%	+0.573	4.904	0.250
07/26/2023	+2.065	-22.7%	+0.516	4.848	0.250
09/20/2023	+1.670	-39.5%	+0.418	4.749	0.250
11/01/2023	+1.106	-56.4%	+0.277	4.608	0.250
12/13/2023	+0.344	-76.2%	+0.086	4.417	0.250
01/31/2024	-0.595	-93.9%	-0.149	4.183	0.250

The Fed has been rapidly tightening monetary policy, but the Fed Funds rate of 4.5% today is still below the historical average of 4.92% dating back to 1971.

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And we understand that drama on Capitol Hill has created plenty of uncertainty, but we like that the calendar has rolled over to the third year of the presidency. History may not repeat, but it often rhymes, and the third year historically has been the best of the four, while a Democrat in the White House and a Split Congress has seen sensational two-year returns, on average, for stocks of all stripes.

THE PRUDENT SPECULATOR

Figure 6:
The Third Year Stands Out from the Others

From 12.31.1928 through 12.31.2021. Geometric average. SOURCE: Kovitz Investment Group using data from Professors Eugene F. Fama and Kenneth R. French

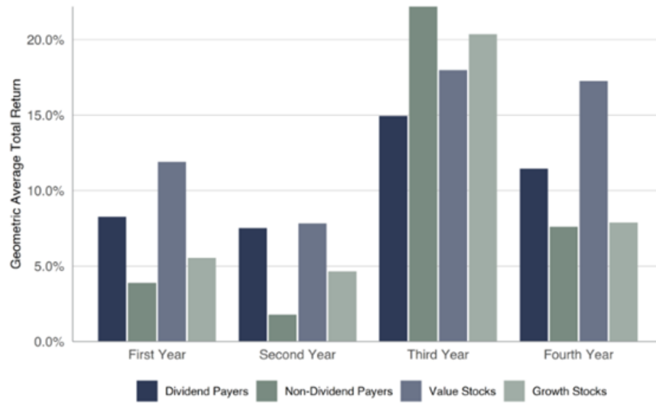


Figure 9:
Investors Seem to be Rewarded by Democrats

Two-year, non-annualized total return. Geometric Average. SOURCE: Kovitz Investment Group using data from Morningstar and Professors Eugene F. Fama and Kenneth R. French

Party Control & Two-Year Returns

President Party	Congress Party	Dividend Payers	Non-Dividend Payers	Value Stocks	Growth Stocks	Large Cap Stocks	Small Cap Stocks
Democrat	Republican	31.9%	21.7%	35.3%	20.8%	32.2%	21.9%
Democrat	Democrat	30.1%	45.7%	45.1%	35.6%	27.4%	53.9%
Democrat	Split	33.1%	33.4%	31.4%	31.5%	33.5%	30.7%
Republican	Republican	-6.8%	-20.3%	-5.7%	-12.9%	-7.1%	-9.9%
Republican	Democrat	20.6%	4.5%	22.5%	14.1%	19.9%	13.1%
Republican	Split	13.9%	-6.7%	21.7%	4.0%	11.8%	11.0%

Washington is likely to cause plenty of consternation as we move through 2023, but the historical evidence would suggest it could be a good year for stocks.

Of course, we realize that Janet Yellen warned on the disastrous ramifications if Congress does not raise the nation's debt ceiling. The Treasury Secretary said last week, "If that happened, our borrowing costs would increase and every American would see that their borrowing costs would increase as well. On top of that, a failure to make payments that are due, whether it's the bondholders or to Social Security recipients or to our military, would undoubtedly cause a recession in the U.S. economy and could cause a global financial crisis."

Certainly, this sounds ominous, but this is not the first time we have had the debt ceiling hanging over our heads. In fact, as the Treasury's website (https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/debt-limit) states, "Since 1960, Congress has acted 78 separate times to permanently raise, temporarily extend, or revise the definition of the debt limit – 49 times under Republican presidents and 29 times under Democratic presidents. Congressional leaders in both parties have recognized that this is necessary."

No doubt, a U.S. default is not something we want to see and we understand that the Treasury is taking emergency steps to keep the proverbial engine running, likely for the next five months, but here is what we wrote on the subject back in August 2011:

The debt drama in Washington is no doubt top of mind for almost every investor. Though there were initially hopes for some sort of a 'Grand Plan' to be struck that might see upwards of $4 trillion cut over 10 years from the country's massive deficit, the warring parties are now trying to simply cobble something together to stave off a default prior to the somewhat arbitrary August 2nd deadline for raising the debt ceiling. As if this weren't enough of a concern, the ratings agencies have suggested that the nation's AAA credit rating may be downgraded even if some sort of a decent compromise is reached. Needless to say, few are happy with our supposed 'leaders', no matter which side of the aisle they may reside.

Not surprisingly, the political rancor has most folks on edge with reports surfacing that investors have been pulling cash from money market funds while the equity markets have been wobbling. Certainly, we do not want to make light of the debt issue, but we continue to think it highly unlikely that Uncle Sam will default on his obligations. Yes, there is a good chance that the U.S. credit rating will be downgraded, but we doubt that we will see a big change in the yields on Treasuries. The reason for this is that there is little place else for investors to go as those seeking the safety and yield of a supposedly risk-free (assuming the security is held to maturity) asset are unlikely to bail out of their Treasury investments.

Don't believe me? Take a look at where things stand on the benchmark 10-Year U.S. Treasury as of July 29. Clearly, if investors thought that there was a risk of the government not making good on its interest and principal payments, yields would have spiked significantly higher, rather than touching their low for the year at 2.80%.

And, believe it or not, we've been down this road before. Consider the following commentary:

Republicans in Congress have vowed not to raise the debt ceiling until the President agrees to their plans to trim federal spending. The President has said he will not be blackmailed into agreeing to the GOP program.

The Treasury Secretary has said it is irresponsible for Republicans to hold the debt ceiling hostage in the budget debate because even the risk of a government default on its debt could cause turmoil in financial markets

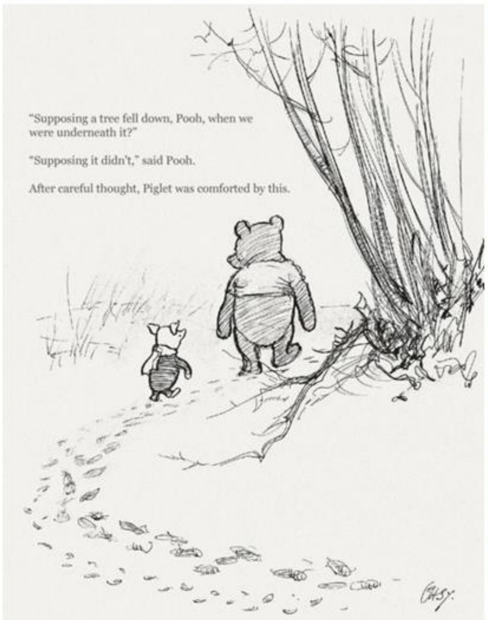
"For all their loose talk," Mr. Clinton said, "the Congressional leaders know that if they were to allow us to go into default, this would have a severe impact on our economy, on financial markets, and on the interest rates paid by government, business and homeowners."

Hopefully, the quote from President Clinton gave away that the time period was November 1995 when the U.S. government had to put non-essential government workers on furlough and suspend non-essential services. While not quite the same situation we are facing today, the debt ceiling was the big sticking point back then and Washington was actually able to reopen for business five days after the initial 'non-essential' measures were taken. Of course, a deal still *could not be reached and the government actually shut down completely four weeks later in an event that lasted from December 16, 1995 to January 6, 1996. Treasuries performed very well (yields actually moved lower!) during that turbulent time.*

But stocks must have taken it on the chin, right? Well, there were definitely some rocky periods, but equities moved nicely higher with the large-cap S&P 500 advancing more than 15% from August 1995 through February 1996!

At the end of the day, we do expect some sort of deal on the debt ceiling to be reached, but we should point out that the S&P 500 has had a 285% total return, or 12.45% per annum, since the July 2011 debt-ceiling scare, and a 1079% total return, or 9.42% per annum, since the one in 1995.

No doubt, there is plenty about which to worry today, including the war in Ukraine, supply-chain disruptions, inventory management woes, corporate-profit question marks, higher inflation readings, the slowing economy and increased risk of recession, not to mention comments and actions from the Federal Reserve, and the debt-ceiling, but history is filled with plenty of frightening events, yet equities have provided handsome rewards…for those who have stuck with them.



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%	45667%
Truman Upset Victory	11/2/1948	11/10/1948	16.70	15.00	-10%	8%	52%	62%	26384%
Korean War	6/23/1950	7/13/1950	19.14	16.69	-13%	32%	45%	153%	23702%
Eisenhower Heart Attack	9/23/1955	9/26/1955	45.63	42.61	-7%	8%	17%	25%	9223%
Suez Canal Crisis	10/30/1956	10/31/1956	46.37	45.58	-2%	-10%	26%	51%	8616%
Sputnik	10/3/1957	10/22/1957	43.14	38.98	-10%	31%	37%	41%	10091%
Cuban Missile Crisis	8/23/1962	10/23/1962	59.70	53.49	-10%	36%	72%	78%	7327%
JFK Assassination	11/21/1963	11/22/1963	71.62	69.61	-3%	24%	14%	53%	5607%
MLK Assassination	4/3/1968	4/5/1968	93.47	93.29	0%	8%	8%	16%	4158%
Kent State Shootings	5/4/1970	5/14/1970	79.00	75.44	-5%	35%	40%	22%	5166%
Arab Oil Embargo	10/18/1973	12/5/1973	110.01	92.16	-16%	-28%	12%	6%	4211%
Nixon Resigns	8/9/1974	8/29/1974	80.86	69.99	-13%	24%	38%	56%	5576%
U.S.S.R. in Afghanistan	12/24/1979	1/3/1980	107.66	105.22	-2%	30%	31%	56%	3676%
Hunt Silver Crisis	2/13/1980	3/27/1980	118.44	98.22	-17%	37%	55%	83%	3945%
Falkland Islands War	4/1/1982	5/7/1982	113.79	119.47	5%	39%	51%	147%	3225%
U.S. Invades Grenada	10/24/1983	11/7/1983	165.99	161.91	-2%	4%	52%	69%	2354%
U.S. Bombs Libya	4/15/1986	4/21/1986	237.73	244.74	3%	20%	27%	57%	1523%
Crash of '87	10/2/1987	10/19/1987	328.07	224.84	-31%	23%	39%	85%	1667%
Gulf War Ultimatum	12/24/1990	1/16/1991	329.90	316.17	-4%	32%	50%	92%	1156%
Gorbachev Coup	8/16/1991	8/19/1991	385.58	376.47	-2%	11%	23%	77%	955%
ERM U.K. Currency Crisis	9/14/1992	10/16/1992	425.27	411.73	-3%	14%	42%	132%	865%
World Trade Center Bombing	2/26/1993	2/27/1993	443.38	443.38	0%	5%	46%	137%	796%
Russia Mexico Orange County	10/11/1994	12/20/1994	465.79	457.10	-2%	33%	107%	210%	769%
Oklahoma City Bombing	4/19/1995	4/20/1995	504.92	505.29	0%	28%	122%	184%	686%
Asian Stock Market Crisis	10/7/1997	10/27/1997	983.12	876.99	-11%	21%	57%	2%	353%
Russian LTCM Crisis	8/18/1998	10/8/1998	1,101.20	959.44	-13%	39%	11%	8%	314%
Clinton Impeachment	12/19/1998	2/12/1999	1,188.03	1,230.13	4%	13%	-10%	-6%	223%
USS Cole Yemen Bombings	10/11/2000	10/18/2000	1,364.59	1,342.13	-2%	-20%	-23%	-12%	196%
September 11 Attacks	9/10/2001	9/21/2001	1,092.54	965.80	-12%	-12%	17%	36%	311%
Iraq War	3/19/2003	5/1/2003	874.02	916.30	5%	21%	42%	54%	334%
Madrid Terrorist Attacks	3/10/2004	3/24/2004	1,123.89	1,091.33	-3%	7%	32%	-26%	264%
London Train Bombing	7/6/2005	7/7/2005	1,194.94	1,197.87	0%	6%	5%	-11%	232%
2008 Market Crash	9/15/2008	3/9/2009	1,192.70	676.53	-43%	69%	103%	178%	487%
Price Changes Only - Does Not Include Dividends				**Averages:**	**-7%**	**18%**	**39%**	**66%**	**5456%**

There have been numerous frightening events over the years, but equities in the fullness of time have overcome all setbacks.

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Obviously, one day does not validate or disprove anything, but Friday's trading illustrated that stocks often climb a Wall of Worry, as the week ended with a big rebound that recouped a significant chunk of the losses for the full four days of trading. This was the case even as *The Wall Street Journal's* front page on Saturday included these headlines:

Google's Parent to Cut 12,000 Jobs
Fed Probes Goldman Over Its Safeguards for Consumer Unit
China's Global Mega-Projects Are Falling Apart
Covid-19 Enters Fourth Year
Home Sales Slip to Cap Worst Year Since 2014

Despite all the negativity, 2023 is still off to a great start, though the 12-month return tallies offer vivid reminder that stock prices move in both directions. While Growth stocks had the upper hand in the latest week, Value has been winning the performance derby for a while now.

Total Returns Matrix

2000	2001		Week	YTD	Since 9.30.22	Last 12 Months	Since 10.31.20	Since 3.23.20	Last 3 Years	Last 5 Years	Name	Symbol
-4.71	-5.44	M	-2.66	0.78	16.92	-1.83	31.65	90.05	21.04	42.76	Dow Jones Industrial Average	INDU Index
1.01	-10.21	A	-0.87	4.01	17.94	-2.80	33.87	92.58	19.76	34.03	New York Stock Exchange Composite	NYA Index
-39.18	-20.81	R	0.55	6.47	5.64	-20.59	3.92	66.09	21.69	59.22	Nasdaq Composite Index	CCMP Index
-22.43	-9.23	K	-0.98	6.42	10.82	-8.83	3.67	67.76	4.85	21.02	Russell 2000 Growth	RU20GRTR Index
22.83	**14.02**	E	**-1.10**	**5.70**	**14.60**	**-4.24**	**49.29**	**117.89**	**21.00**	**24.83**	**Russell 2000 Value**	**RU20VATR Index**
-3.02	2.49	T	-1.04	6.06	12.67	-6.41	24.68	92.86	14.06	24.75	Russell 2000	RU20INTR Index
-11.75	-20.15		-0.05	5.25	12.51	-10.70	3.35	71.40	13.16	43.74	Russell Midcap Growth Index Total Return	RUMCGRTR Index
19.18	**2.33**		**-1.17**	**4.61**	**15.55**	**-3.65**	**40.92**	**115.40**	**21.74**	**34.54**	**Russell Midcap Value Index Total Return**	**RUMCVATR Index**
8.25	-5.62	O	-0.78	4.83	14.46	-6.02	26.61	100.65	21.09	41.96	Russell Midcap Index Total Return	RUMCINTR Index
-22.42	-19.63	F	0.29	4.87	7.30	-17.03	8.83	74.63	23.69	62.52	Russell 3000 Growth	RU30GRTR Index
8.04	**-4.33**		**-1.45**	**3.10**	**15.66**	**-2.67**	**40.88**	**96.91**	**20.74**	**35.92**	**Russell 3000 Value**	**RU30VATR Index**
-7.46	-11.46	S	-0.61	3.96	11.43	-10.09	23.71	86.63	23.73	50.87	Russell 3000	RU30INTR Index
9.64	-0.39	T	-1.04	4.41	16.56	-3.19	42.85	116.00	32.13	54.55	S&P 500 Equal Weighted	SPXEWTR Index
-9.10	-11.89	O	-0.65	3.55	11.38	-9.90	25.74	85.73	25.28	54.43	S&P 500	SPXT Index
-22.08	-12.73	C	0.16	2.99	4.48	-19.59	9.59	71.51	22.27	58.19	S&P 500 Growth	SPTRSGX Index
6.08	**-11.71**		**-1.50**	**4.15**	**18.31**	**0.50**	**44.04**	**95.86**	**23.36**	**44.12**	**S&P 500 Value**	**SPTRSVX Index**
3.18	1.57	K	0.00	3.33	8.03	-12.45	-14.90	-7.26	-9.77	-5.37	Bloomberg Barclays Global-Aggregate Bond	LEGATRUU Index
11.63	8.44	S	0.15	2.89	4.82	-8.60	-10.89	-6.23	-5.74	3.98	Bloomberg Barclays U.S. Aggregate Bond	LBUSTRUU Index

As of 1.20.23. Source Kovitz using data from Bloomberg

It is a market of stocks and returns over the last couple of years show wide dispersion, similar in magnitude to what was seen after the bursting of the Tech Bubble in the year 2000.

Needless to say, we think time in the market trumps market timing, as even those compensated to pontificate on the short-term gyrations in stocks often end up making little sense.

For example, here are comments published on *CNBC.com* from one professional market watcher endeavoring to explain Friday's rally:

"We're having a more emotional reaction that expected. A lot of people got so pessimistic and we saw parabolic moves to kick off the year. Now, as expected, the markets aren't going in a straight line."

"We are finding a way to continue to move and have higher lows. The higher lows put a little bit of confidence in the bulls. However, the technicals are still favoring the bears and selling rallies. You're seeing more weight go into some of the beat-up technology and because people are becoming a little bit more thoughtful of opportunity in the absolute tech wreck we saw in 2022."

Clear as mud from where we sit!

Anything can happen as we move forward, so we'll leave the short-term predictions to the soothsayers and fortune tellers. 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.

THE PRUDENT SPECULATOR

Advancing Markets

Minimum Rise %	Average Gain	Average # Days	Count	Frequency (in Years)	Last Start	Last End
20.0%	113.4%	995	27	3.4	3/23/2020	1/3/2022
17.5%	68.2%	583	39	2.3	3/23/2020	1/3/2022
15.0%	65.7%	555	46	2.0	6/16/2022	8/16/2022
12.5%	44.3%	332	74	1.3	10/12/2022	11/30/2022
10.0%	34.8%	243	101	0.9	10/12/2022	11/30/2022
7.5%	23.6%	148	160	0.6	10/12/2022	11/30/2022
5.0%	14.7%	72	315	0.3	12/28/2022	1/13/2023

Declining Markets

Minimum Decline %	Average Loss	Average # Days	Count	Frequency (in Years)	Last Start	Last End
-20.0%	-35.0%	281	27	3.4	1/3/2022	6/16/2022
-17.5%	-30.2%	216	39	2.4	1/3/2022	6/16/2022
-15.0%	-28.0%	185	46	2.0	8/16/2022	10/12/2022
-12.5%	-22.7%	137	73	1.3	8/16/2022	10/12/2022
-10.0%	-19.6%	101	100	0.9	8/16/2022	10/12/2022
-7.5%	-15.5%	65	159	0.6	8/16/2022	10/12/2022
-5.0%	-10.9%	36	314	0.3	11/30/2022	12/28/2022

From 02.20.28 through 1.13.23. S&P 500 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	13.2%	26.0%
Growth Stocks	9.5%	21.4%
Dividend Paying Stocks	10.7%	18.1%
Non-Dividend Paying Stocks	8.8%	29.3%
Long-Term Gov't Bonds	5.1%	8.7%
Intermediate Gov't Bonds	4.9%	4.3%
Treasury Bills	3.2%	0.9%
Inflation	3.0%	1.8%

From 06.30.27 through 11.30.22. 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

The secret to success in stocks is not to get scared out of them as every downturn has been followed by an upswing of far greater magnitude, so much so that long-term returns for Value stocks have exceeded 13% per annum.

We are always braced for downside volatility, but we see no reason to alter our long-term enthusiasm for our broadly diversified portfolios of what we believe to be undervalued stocks.

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	12.2	12.3	0.8	2.3	2.8
ValuePlus	12.8	12.8	1.2	2.4	2.4
Dividend Income	11.9	12.3	0.7	2.1	3.3
Focused Dividend Income	13.1	13.3	1.1	2.5	2.8
Focused ValuePlus	13.3	13.4	1.3	2.6	2.6
Small-Mid Dividend Value	11.0	10.6	0.5	1.7	2.8
Russell 3000	20.6	18.1	2.1	3.7	1.7
Russell 3000 Growth	28.4	22.8	3.0	9.1	1.0
Russell 3000 Value	16.4	15.1	1.6	2.4	2.2
Russell 1000	19.9	17.9	2.2	3.9	1.7
Russell 1000 Growth	26.7	22.6	3.3	9.4	1.1
Russell 1000 Value	16.0	15.0	1.7	2.5	2.2
S&P 500 Index	19.3	17.8	2.3	4.0	1.7
S&P 500 Growth Index	19.8	18.9	3.2	6.8	1.4
S&P 500 Value Index	18.7	16.7	1.8	2.7	2.0
S&P 500 Pure Value Index	11.3	11.0	0.7	1.6	2.5

As of 01.21.23. 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.

We sleep very well at night, given the inexpensive valuation multiples and generous dividend yields associated with our managed account portfolios.

Stock Updates

Keeping 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/. We also offer the reminder that any sales we make for our newsletter strategies are announced via our *Sales Alerts*.

Jason Clark, Chris Quigley and Zack Tart take a look at earnings reports and other market-moving news of note out last week for more than a few of our recommendations.

Via press release on Thursday afternoon, high-end department store **Nordstrom** (JWN – $17.47) offered a weak holiday sales report and cut its outlook, sending shares skidding more than 7% in after-hours trading. Apparently, the bad news didn't make it to traders on Friday, where the stock eventually finished up two cents, though the day was broadly positive overall.

Companywide net sales decreased by 3.5% for the holiday period, compared to the same period a year ago. Nordstrom banner sales fell 1.7%, while the company's Rack discount brand tumbled 7.6%. "Having a healthier inventory level and mix positions us well to react quickly to changing consumer demand," said Pete Nordstrom, president and chief brand officer of Nordstrom, Inc. "Given the continued uncertain environment, we remain focused on executing with flexibility and agility, including conservative buy plans and faster inventory turns. We continue to enhance our customer experience with our *Closer to You* strategy, which links our digital and physical assets. Additionally, we are further optimizing our supply chain to improve the customer experience and expense efficiency, and we expect these initiatives will continue to deliver significant benefits in 2023."

Updates to the company's 2022 guidance for revenue growth, including retail sales and credit card revenue, at the low-end of its previously issued outlook of 5% to 7%, as well as adjusted EPS, excluding the impact of share repurchase activity, if any, of $1.50 to $1.70, compared with its prior outlook of $2.30 to $2.60. The final Q4 report is due on March 2.

No doubt, the lowering of guidance is not a grand development, but the stock was already trading for a deeply discounted valuation, and the mid-point of the updated EPS forecast puts the forward P/E ratio in the 11 range. Further, we expect the bottom line to improve in the years ahead, given that supply-chain problems and the inventory difficulties they caused should dissipate. Nordstrom also has long been a takeover candidate, though the poison pill plans the company adopted last September to head off pressure from a passive 9.8% interest acquired by Mexican peer Liverpool puts a [temporary] wet blanket on that possibility.

Of course, our interest in JWN is based on long-term capital appreciation (our Target Price is $31) and income (the dividend yield is now 4.4%) potential, so we are hoping that a fire sale does not occur. True, there seems to be some reworking necessary in the Rack business, but the flagship stores have come back to life, so we are content to hold our current position, though we are pleased that our partial-sale strategy allowed us to take profits on our JWN holdings at much higher prices back in early-2021.

The release of bank earnings resumed last week as diversified financial titans **Goldman Sachs** (GS – $341.84) and **Morgan Stanley** (MS – $96.24) kicked off the parade and reports from regional banks trickled in throughout the week.

Goldman earned an adjusted $3.94 (vs. $3.96 est.) on $10.6 billion of revenue. investment banking and advisory segments remained under pressure, offset by 44% growth in FICC sales and trading. Plenty of headlines have noted the firm's efforts to downsize, but the 3,200 planned layoffs weren't enough to meet the Street's expense expectations given an expense ratio of 76.4% (vs. 68.5%).

A series of reorganizations in promotion of, but now backing a way from, its consumer division that have been widely publicized have no doubt occupied plenty of management's time. When asked by an analyst "What went wrong?" CEO David Solomon responded, "I think it's a fair question is we tried to do too much too quickly. And of course, in the environment that we're in it's hard to go back when we started in that strategy. Six years ago, we obviously had both the deposit business and loan business and we talked about a much broader platform. And I think we came to the conclusion, that there were some changes."

He added, "One of the big changes that affect the pace of the ability to do this and it's different in scaling things like this is CECL is a big change. CECL changed the curve on growing these lending businesses at scale from scratch. So we had to adjust to that. The regulatory environment has also changed over the course of the last couple of years. But I think it became clear to us early in 2022 that we were doing too much, it was affecting our execution, I think we probably in some places haven't had all the talent that we've needed to execute the way we've wanted, we're making adjustments on that."

Mr. Solomon also reminded, "Despite a more challenged fourth quarter performance, we delivered for shareholders in 2022. We generated double-digit returns in a year or rapid monetary tightening and ongoing macro uncertainty drove significant market disruption, with both equity and fixed income markets falling for the first time in over 50 years. We grew management other fees by 13% year-over-year and grew net interest income by 19%…We reduced on-balance sheet alternative investments by $9 billion. We also returned $6.7 billion of capital in the form of dividends and share repurchases, and we grew our book value by 7%. This brings our book value growth since our first Investor Day to almost 40%, roughly twice as much as our next closest competitor."

We think Goldman will rebound from 2022, which was a rocky year for most investable assets and as corporate America adjusts to a higher cost of capital. The company remains tremendously profitable, while shares trade for an inexpensive 10 times NTM EPS estimates and offer a 2.9% dividend yield. Of course, the company received more bad news on Friday when it was reported that the Federal Reserve is investigating its consumer businesses, with the agency concerned that improper monitoring and control systems were in place. That wasn't what we wanted to hear to end the week, but we think Goldman will get the consumer mess resolved and our Target Price now stands at $434.

The story was largely similarly at Morgan Stanley as revenue for the Investment Banking and Trading segments declined versus the prior year. Wealth Management was a major bright spot, however, and actually saw an increase in revenue of 6% in Q4 year-over-year despite market volatility as the reduction in assets under management was offset by higher net interest income within the segment. The net result was $1.31 of adjusted EPS (vs. 1.23 est.) supporting future returns of capital to shareholders as MS digests purchases of E*TRADE and Eaton Vance in recent years. Investors liked what they heard as MS shares advanced 5% on the week.

CEO James Gorman said the bank is focused on keeping expenses in check but added "We also want to feed the beast. I mean, we're growing parts of this firm. We're trying to — we don't — we're not of the view that we're heading into a dark period, whatever negativity in the world is out there. That's not our house views. So, we want to make sure we're positioned for growth. This thing will turn. M&A underwriting will come back. I'm positive of it. So we want to be well positioned for it."

Management repurchased 6% of the stock in 2022 in addition to paying a dividend where the yield is now 3.2%. Mr. Gorman & Co. endeavor to add $1 trillion of net new assets under management every three years with a long-term goal of reaching $10 trillion.

MS trades for 13 times NTM EPS and our Target Price has been lifted to $117.

Heightened concerns over a potential recession have weighed on bank shares, with the KBW Bank index sliding into a bear market over the past 12 months. Yes, banks are historically exposed to downturns in the economy, given their linkage to the health of consumer and corporate credit. Interestingly, the corresponding Regional Bank index fared better in 2022, dropping less than 10% on a price basis.

But the outlook for the broader sector comes at a time when the upward shift of interest rates has lifted core banking profits tremendously (even higher after adjusting for loan-loss accounting) given wider lending margins and as banks have still been able to grow loans. However, this tailwind has been offset by lighter fee income, ebbing deposits (and rising deposit costs due to competition), higher provisions for loan losses and modestly higher charge-offs. Seven of our regional banks turned in their Q4 report cards last week and we highlight the latest reported financial results below:

Citizens Financial (CFG – $41.26) Q4 Summary

Adjusted EPS $1.32 vs. $1.26 in Q4 ‘21, estimate $1.32
Net interest income $1.7 billion +50.5% vs. Q4 ‘21, estimate $1.7 billion
Net interest margin 3.29% vs. 2.66% in Q4 ‘21, estimate 3.34%
Provision for credit losses $132 million vs. recovery of $25 million in Q4 ‘21, estimate $141.8 million
Net charge-offs $88 million, +96% vs. Q4 ‘21, estimate $85.5 million
Non-interest income $505 billion, -15% vs. Q4 ‘21, estimate $512 billion
Non-interest expense $1.24 billion, +17% vs. Q4 ‘21, estimate $1.22 billion
Common equity Tier 1 ratio 10.0% vs. 9.9% in Q4 ‘21, estimate 9.85%

CEO Bruce Van Saun commented, “We are pleased with the financial performance we delivered for the fourth quarter and the full year, and we feel well-positioned to navigate through an uncertain environment in 2023. We are playing strong defense with a robust balance sheet position and highly prudent credit risk appetite. At the same time, we continue to play disciplined offense with continuing investments in our growth initiatives. We are focused on building out a prudent sustainable growth trajectory over the medium term.”

Turning to 2023, he added, “We assume a slowdown in economic growth to 1% for the year through early Fed rate hikes and Q4 cut and inflation getting below 3% by Q4. We project moderate loan growth, partially offset by continued runoff in our order book of close to $3 billion. Overall, we see solid NII growth as NIM gradually rises to 3.4% over the year, a roughly 8% growth in fees to kind of rebound in capital markets fees over the course of the year. Solid expense discipline with core expense growth ex acquisition and FDIC impacts of 3.5% to 4%.”

Following the purchase of HSBC branches within its market and the acquisition of Investors Bancorp in 2021, Rhode Island-based Citizens has grown its deposit franchise by over 17% year-over-year. We think the moves complement and round out its existing territory, while adding JMP Group (securities) into the fold (also in 2021) brings diversification through additional fee generation. Dealmaking and capital markets activity has slowed, but higher net interest spreads and a focus on maximizing operating leverage for an expanded operation prime the bank for higher returns in the current year. Shares trade for a single-digit estimated P/E ratio and offer a 4.1% dividend yield. Our Target Price is $69.

PNC Financial (PNC – $154.87) Q4 Summary

Adjusted EPS $3.49 vs. $3.68 in Q4 '21, estimate $3.96
Net interest income $3.68 billion, +29% vs. Q4 '21, estimate $3.64 billion
Net interest margin 2.92% vs. 2.27% in Q4 '21, estimate 3.00%
Provision for credit losses $408 million vs. recovery of $327 million in Q4 '21, estimate $262.8 million
Net charge-offs $224 million, +81% vs. Q4 '21, estimate $141.6 million
Non-interest income $2.08 billion, -8.2% vs. Q4 '21, estimate $1.98 billion
Non-interest expense $3.5 billion, -8.4% vs. Q4 '21, estimate $3.3 billion
Common equity Tier 1 ratio 9.1% vs. 10.2% vs. Q4 '21, estimate 9.41%

CEO Bill Demchak said, "Importantly, as the credit environment continues to trend towards normalized levels, our overall credit quality metrics remained solid. I'd add that with charge-offs having been so low, it's not surprising to see volatility quarter-to-quarter. And we saw this in the fourth quarter with an out-sized loss on one commercial credit pushing us outside of our expected range. During the quarter, we returned $1.2 billion of capital to shareholders through share repurchases and dividends, bringing our total annual capital return to $6 billion. Our progress within the BBVA influence markets continues to exceed our expectations and we see powerful growth opportunities across our lines of business in these new markets. We continue to generate new customer relationships and we've been thrilled with the quality of bankers we've been able to hire."

He concluded, "In summary, it was a solid fourth quarter. As we further built on our post-acquisition momentum, delivered for our customers and communities across the country, generated strong financial results for our shareholders and put ourselves in a position of strength as we move into 2023."

We continue to like PNC's latest acquisitions, which give the Pittsburgh-based company expanded access to 29 of the top 30 Metropolitan Statistical Areas across the country. Management says that there continues to be momentum for new product sales. Shares have modestly lagged peers since the beginning of 2022, and the stock was off over 5.5% last week, but we view this as an opportunity for those looking to add to banking exposure. PNC trades for about 10 times NTM adjusted EPS expectations and we like the solid long-term potential from current levels. We also think PNC has an opportunity to become more efficient over the next few years. The dividend yield now sits at 3.9% and our Target Price stands at $229.

Truist Financial (TFC – $47.92) Q4 Summary

Adjusted EPS $1.30 vs. $1.38 in Q4 ‘21, estimate $1.29
Net interest income $4.03 billion, +23% vs. Q4 ‘21, estimate $3.95 billion
Net interest margin 3.25% vs. 2.76% in Q4 ‘21, estimate 3.23%
Provision for credit losses $467 million vs. recovery of $103 million in Q4 ‘21, estimate $354.5 million
Net charge-offs $273 million, +50% vs. Q4 ‘21, estimate $257.1 million
Non-interest income $2.23 billion, -4.1% vs. Q4 ‘21, estimate $2.22 billion
Common Equity Tier 1 ratio 9% vs. 9.6% in Q4 ‘21, estimate 9.14%

CEO Bill Rodgers explained, “Net interest income reached a new high supported by strong loan growth and significant margin expansion resulted from higher short-term rates and well-controlled deposit costs.”

CFO Mike Maguire said expense growth was a “result of the increase in the minimum wage, investments in revenue-generating businesses technology and acquisitions, higher call center staffing to support our clients’ post-merger in a normalizing T&E spend.”

Mr. Rodgers added, “The pivot from integrating to operating is real, it’s palpable, and it can be evidenced across a number of dimensions. Loan production in the fourth quarter was near the highest it’s been at Truist.”

We continue to find the marriage of Southeastern banking leaders BB&T and SunTrust that created Truist to be favorable, given the conservative lending culture and competitive brands that both had independently, and the potential for cost savings. We think TFC trades at an attractive forward P/E ratio just below 10, and we like that the southeastern U.S. has benefitted from recent migration patterns. The dividend yield is 4.3% and our Target Price now resides at $68.

Fifth Third Bancorp (FITB – $34.61) Q4 Summary

EPS $1.01 vs. $0.90 in Q4 ’21, estimate $0.99
Net interest income $1.58 billion, +32% vs. Q4 ‘21, estimate $1.57 billion
Net interest margin 3.35% vs. 2.55% in Q4 ‘21, estimate 3.36%
Provision for credit losses $180 million vs. recovery of $47 million in Q4 ‘21, estimate $177 million
Net charge-offs $68 million vs. $68 million in Q4 ‘21, estimate $71.7 million
Non-interest income $777 million, -6.3% vs. Q4 ‘21, estimate $764.2 million
Non-interest expenses $1.22 billion vs. $1.21 billion in Q4 ’21, estimate $1.2 billion
Common equity Tier 1 ratio 9.27% vs. 9.53% vs. Q4 ‘21, estimate 9.1%

CEO Tim Spence said, “During 2022, we remain focused on delivering stable long-term results instead of chasing short-term earnings. We maintained our discipline in our credit underwriting with continued focus on granularity and diversification. The outcomes of this are evident in our NPA, NPL and early-stage delinquency ratios, all of which have remained well behaved and well below normalized levels.”

He added, “Our balance sheet management approach remains centered on providing strong and stable NII performance across various rate environments. We extended our advantage in our securities yield by waiting to deploy excess liquidity until we were able to earn positive real yields, and we added derivatives to provide hedge protection through 2031. These actions will provide significant long-term benefits in the event of a lower rate environment.”

Management expects to deploy about $1 billion toward share repurchases in 2023, backed by full-year growth in net interest income between 13% to 14%.

KeyCorp (KEY – $17.44) Q4 Summary

EPS $0.38 vs. $0.64 in Q4 ‘ 21, estimate $0.55
Revenue $1.90 billion, -2.5% vs. Q4 ‘21, estimate $1.93 billion
Net interest income $1.22 billion, +18% vs. Q4 ‘21, estimate $1.25 billion
Net interest margin 2.73% vs. 2.44% in Q4 ‘21, estimate 2.88%
Provision for credit losses $265 million vs. $4 million in Q4 ‘21, estimate $115.2 million
Net charge-offs $41 million vs. $19 million in Q4 ‘21, estimate $48.7 million
Non-interest income $671 million, -26% vs. Q4 ‘21, estimate $671 million
Non-interest expenses $961 million, -17.9% vs. Q4 ‘21, estimate $1.13 billion
Common equity Tier 1 ratio 9.1% vs. 9.5% vs. Q4 ‘21, estimate 8.99%

CEO Chris Gorman commented, “In 2023, we will continue to execute on our differentiated business model and strategy. We will focus on expanding our presence in our fastest-growing markets and targeted industry verticals. As we demonstrated again in 2022, we are uniquely positioned to support clients through various market conditions. Secondly, we will continue to benefit from our balance sheet and interest rate positioning. We have been very deliberate and intentional in the manner in which we have managed our interest rate risk with a longer-term perspective.”

Regarding KEY’s credit quality, he added, “We’ve spent the last decade derisking our portfolio, positioning the company to outperform through the business cycle. Despite our strong credit metrics, we’ve built our loan loss reserve this quarter which using our 2023 net charge-off outlook now represents almost five years of coverage. To put this in perspective, our reserve is now above our CECL day one level while non-performing loans and delinquencies are roughly 1/2 of our pre-pandemic levels.”

We continue to appreciate having midwestern-based exposure through KEY and FITB, given their conservative underwriting culture, owing to lessons learned from the Great Financial Crisis. While interest income growth outlooks are tempered for both banks from here, they each boast diverse revenue streams with healthy fee generation potential. KEY and FITB trade for 8 and 9 times respective NTM EPS estimates with respective dividend yields of 4.7% and 3.8%. Our Target Price for KEY is $27 and for FITB is $49.

Comerica Inc (CMA – $69.13) Q4 Summary

EPS $2.58 vs. $1.66 in Q4 '21, estimate $2.54
Net interest income $742 million, +61% vs. Q4 '21, estimate $739.6 million
Net interest margin 3.74% vs. 2.04% in Q4 '21, estimate 3.92%
Provision for credit losses $33 million vs. recovery of $25 million in Q4 '21, estimate $32.2 million
Non-interest income $278 million, -3.8% vs. Q4 '21, estimate $269.2 million
Non-interest expense $541 million, +11.3% vs. Q4 '21, estimate $518.4 million
Common equity Tier 1 ratio 10.0% vs. 10.2% in Q4 '21, estimate 9.82%

CFO James Herzog said, "We project strong net interest income, up 17% to 20% over our record 2022 level, which reflects the full-year benefit from higher rates and we are assuming rates follow the 12/31 forward curve. First quarter will be impacted by two fewer days, seasonal deposit outflows and continued deposit pricing actions. We expect net interest income to increase through the year as we continue to benefit from rising rates and loan growth in conjunction with expanding relationships and acquiring new customers. Credit quality has been excellent and we expect it to remain strong. Therefore, we forecast net charge-offs at the lower end of our normal range of 20 basis points to 40 basis points. Assuming the economy performs in line with our expectations, we expect a gradual normalization in credit metrics and our reserve level."

Historically one of our most interest rate sensitive banks, it's no major surprise to see such a boost to net interest income in the latest quarter. The jump in deposit costs to 97 basis points from 20 basis points in Q3 was notable and also to be expected, although it is something to watch in future quarters as the Fed's tightening regime evolves. Even as deposits become more competitive, Comerica still has plenty of lending capacity as current loans represent just 75% of current deposits. Shares are within a stone's throw of their price at the time of our last writing and remain attractive at 7 times NTM EPS estimates. The dividend yield is now 3.9% and our Target Price remains at $105.

Bank OZK (OZK – $43.13) Q4 Summary

EPS $1.34 vs. $1.17 in Q4 '21, estimate $1.32
Net interest income $334.9 million, +25% vs. Q4 '21, estimate $314 million
Net interest margin 5.46% vs. 4.41% in Q4 '21, estimate 5.25%
Provision for credit losses $33 million vs. recovery of $8 million in Q4 '21, estimate $14.7 million
Net charge-offs $2.9. million vs. $1.8 million in Q4 '21, estimate charge-off $6.0 million
Non-interest income $27.5 million, -7.2% vs. Q4 '21, estimate $26.4 million
Non-interest expense $119 million, +8.1% vs. Q4 '21, estimate $118.2 million
Common equity Tier 1 ratio 13.7% vs. 14.8% in Q4 '21, estimate 13.5%

CEO George Gleason commented, "We are pleased to report our strong results for the fourth quarter and full year of 2022. Our high level of profitability, strong capital and liquidity, disciplined credit culture and outstanding team have us well positioned for the current environment and the longer term."

In 2022, management repurchased approximately 8.37 million shares (roughly 10% of shares outstanding) for $350.0 million in addition to recently increasing the dividend for the 50th consecutive quarter.

We continue to favor Bank OZK's strategy of growth through the slow building and acquisition of individual branches rather than the consolidation of entire banks. Mr. Gleason has stated this strategy makes culture assimilation easier, likely contributing to an impressive efficiency ratio that ticked lower in Q4 to among the lowest in our coverage universe at 32.8%. We also like the unique exposure OZK offers to commercial and industrial lending, a typically more volatile segment of banking, as it has been able to produce above average net interest margins while experiencing mild loan losses (relative to peers) throughout its history. With a dividend yield of 3.2% and a NTM P/E of 8, our Target Price for OZK shares has been adjusted to $66.