Market Commentary Monday, April 17, 2023

April 16, 2023

EXECUTIVE SUMMARY

Newsletter Trades – 1 Fix for TPS Portfolio
Contra-Indicator – AAII Bulls Skid
Wall of Worry – Stock Have Overcome Plenty of Disconcerting News in the Fullness of Time
Fed News – Disconnect Between Minutes and Press Conference / GDP Projections
Weaker-than-Expected Econ Stats – Retail Sales & Jobless Claims
Better-than-Forecast Econ Numbers – Sentiment & Industrial Production
Earnings – Healthy Corporate Profits in ’23 and ’24 Still the Projection
Inflation – Sharply Lower CPI & PPI
Valuations – Still Liking the Metrics for our Portfolios
Recessions – History Shows No Reason, On Average, for Long-Term-Oriented Investors to Sell Stocks
Stock News – Update on MU, GBX, BLK, PNC, C & JPM

Market Review

As discussed in last week’s *Market Commentary*, we sold 223 **Bank of New York Mellon** (BK – $46.36) at $45.04 and we bought 358 **Bank of America** (BAC – $29.52) at $27.9042 for TPS Portfolio on Monday, April 10.

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If we were going to blame the pullback during the first week of April on the good folks at the American Association of Individual Investors (AAII) becoming much more optimistic about the prospects for stocks over the ensuing six months, we suppose we should credit last week’s rebound to a renewed sense of pessimism on the contrarian AAII Sentiment gauge. Interestingly, while the AAII tally of Bears edged down 0.5 percentage points to 34.5%, the count of Bulls fell by 7.2 percentage points to 26.1%, with the Bull-Bear spread sinking to -8.4% from -1.7% the week prior.

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 = 7.00										
BELOW	-54.0	7.0	931	0.24%	0.20%	1.15%	1.01%	3.30%	2.91%	6.44%	5.68%
ABOVE	7.0	62.9	929	0.17%	0.16%	0.53%	0.44%	2.00%	1.75%	4.64%	4.15%
	Ten Groupings of 1860 Data Points										
1	-54.0	-17.0	188	0.41%	0.34%	2.12%	1.88%	4.61%	4.09%	8.38%	7.19%
2	-17.0	-9.0	184	0.23%	0.19%	0.90%	0.76%	3.46%	3.08%	6.01%	5.22%
3	-8.9	-2.7	185	0.33%	0.30%	1.02%	0.91%	3.46%	3.06%	7.64%	6.92%
4	-2.6	2.5	186	0.16%	0.12%	0.96%	0.87%	2.27%	1.89%	5.29%	4.73%
5	2.6	7.0	188	0.07%	0.04%	0.72%	0.62%	2.71%	2.45%	4.88%	4.35%
6	7.0	11.4	184	0.20%	0.19%	0.71%	0.63%	2.24%	2.02%	4.98%	4.52%
7	11.4	16.0	188	0.18%	0.16%	0.40%	0.26%	2.18%	1.90%	5.02%	4.50%
8	16.0	21.7	184	0.11%	0.09%	0.87%	0.80%	2.23%	1.99%	5.80%	5.38%
9	21.7	29.0	188	0.15%	0.13%	0.38%	0.30%	1.84%	1.54%	4.80%	4.24%
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 04.13.23. Unannualized. SOURCE: Kovitz using data from American Association of Individual Investors and Bloomberg

The number of Bulls is now well below the 37.5% average and the Bears are above the 31.0% average, with forward returns historically better when the AAII Bull-Bear Spread is tilted heavily toward negativity. Certainly, no metric is infallible, but it is fascinating to see 36 years of historical evidence in the chart above confirming that, on average, it often pays to be greedy when others are fearful.

Of course, there usually is something for investors to be concerned about, as evidenced by all the disconcerting events that have occurred just since the end of the Great Financial Crisis in March 2009, yet stocks, in the fullness of time, always seem to manage to climb a wall of worry.

THE PRUDENT SPECULATOR

Event	Date	S&P End Value	3 Months Later	6 Months Later	12 Months Later	36 Months Later	60 Months Later	Event to Present
Flash Crash	5/6/2010	1,128.15	-1%	9%	19%	43%	84%	267%
Japan Tsunami	3/11/2011	1,304.28	-3%	-12%	5%	43%	55%	217%
S&P Downgrade	8/6/2011	1,199.38	4%	12%	16%	60%	82%	245%
Hurricane Sandy	10/22/2012	1,433.82	4%	9%	22%	43%	80%	189%
Fiscal Cliff	1/1/2013	1,426.19	10%	13%	30%	43%	87%	190%
Taper Tantrum	5/22/2013	1,655.35	0%	9%	14%	24%	65%	150%
Russia and Ukraine	2/20/2014	1,839.78	2%	8%	15%	28%	51%	125%
Ebola Scare	9/4/2014	1,997.65	4%	5%	-4%	24%	47%	107%
Charlie Hebdo	1/7/2015	2,025.90	2%	3%	-4%	35%	60%	104%
Greek Default	6/30/2015	2,063.11	-7%	0%	2%	32%	50%	101%
China Devalues Yuan	8/10/2015	2,104.18	-1%	-12%	3%	35%	60%	97%
Paris Bataclan	12/13/2015	2,012.37	0%	3%	13%	32%	82%	106%
U.S. Interest Rate Hike	12/16/2015	2,073.07	-2%	0%	9%	25%	79%	100%
China GDP Slowing	1/19/2016	1,881.33	12%	15%	20%	42%	102%	120%
Brexit Vote	6/23/2016	2,113.32	2%	7%	15%	40%	101%	96%
Trump Victory	11/8/2016	2,139.56	7%	12%	21%	45%	120%	93%
Trump Trade War	3/2/2018	2,691.25	2%	8%	4%	44%	48%	54%
COVID-19 Pandemic	3/11/2020	2,741.38	10%	22%	44%	41%		51%
Biden Victory	11/3/2020	3,369.16	14%	24%	38%			23%
Georgia Runoff	1/5/2021	3,726.86	9%	17%	26%			11%
Price Changes Only								
Does Not Include Dividends		**Averages:**	**3%**	**8%**	**15%**	**38%**	**74%**	**122%**
Source: Kovitz using data from Bloomberg. As of 4.14.23								

Speaking of worry, last week's rebound was interrupted on Wednesday when the Minutes of the FOMC's March meeting were released. The trouble seemed to be that the Fed staff forecast presented at the meeting anticipated a recession would start later this year due to banking-sector turmoil. However, Jerome H. Powell in his post-meeting Press Conference last month did not state that an economic contraction was his projection.

To be fair, he didn't say that a recession would not occur, but when asked, "Do you still see a possibility of a soft landing for the U.S. economy," the Fed Chair responded:

You know it's, it's too early to say, really, whether these events have had much of an effect. It's hard for me to see how they would have helped the possibility—but I guess I would just say, it's too early to say whether there really have been changes in that. You know, the question will be how long this period is sustained. The longer it's sustained, then the greater will be the likely declines in—or tightening in credit standards, credit availability, so we'll just have to see. I do still think, though, that there's a—there's a pathway to that. I think that pathway still exists and, you know, we're certainly trying to find it.

In addition, the economic projections from Federal Reserve Board Members and Federal Reserve Bank Presidents prepared for that Fed Meeting still called for modest real (inflation-adjusted)

GDP growth of 0.4% this year and 1.2% in 2024. Yes, those were downgrades to the outlook, but they did not predict a contraction on a year-over-year basis.

THE PRUDENT SPECULATOR

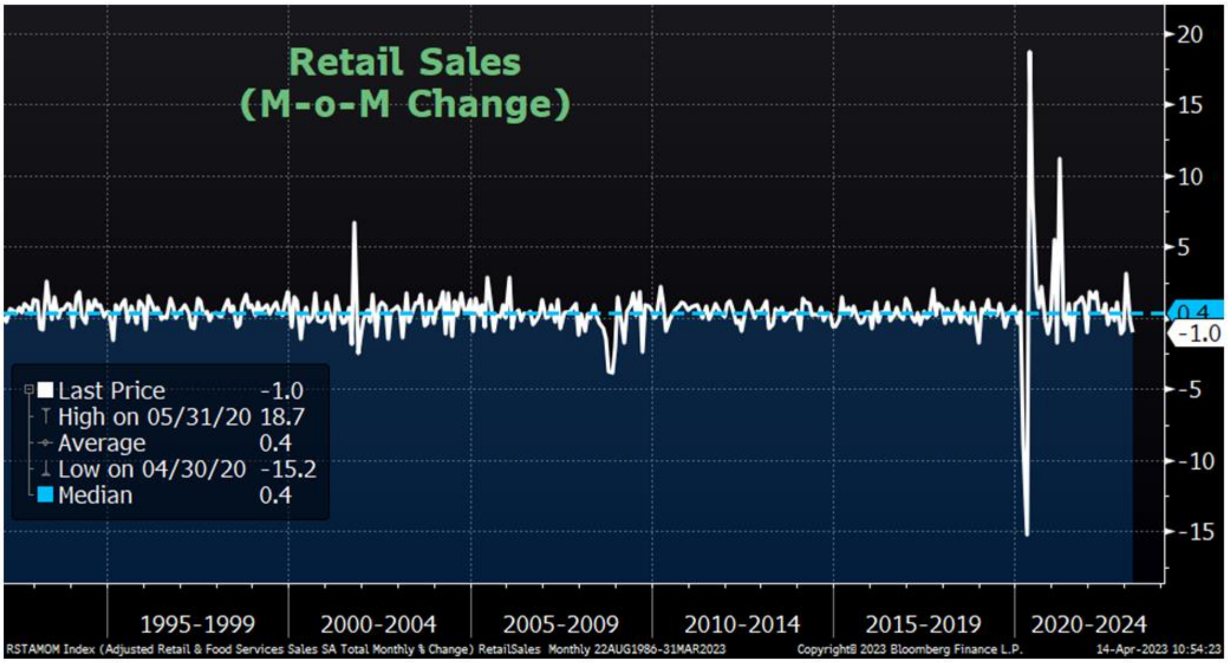
Table 1. Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy, March 2023

Percent

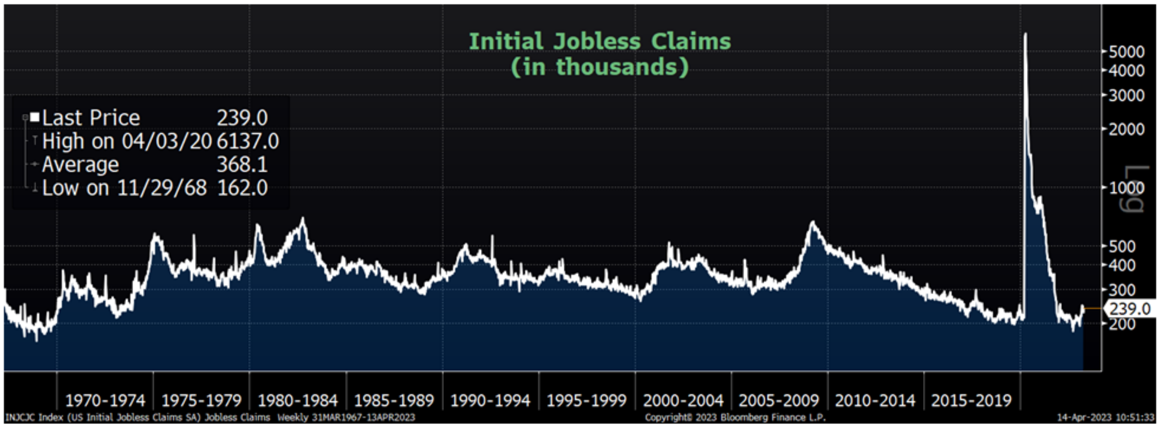
Variable	Median[1]				Central Tendency[2]				Range[3]			
	2023	2024	2025	Longer run	2023	2024	2025	Longer run	2023	2024	2025	Longer run
Change in real GDP	0.4	1.2	1.9	1.8	0.0–0.8	1.0–1.5	1.7–2.1	1.7–2.0	-0.2–1.3	0.3–2.0	1.5–2.2	1.6–2.5
December projection	0.5	1.6	1.8	1.8	0.4–1.0	1.3–2.0	1.6–2.0	1.7–2.0	-0.5–1.0	0.5–2.4	1.4–2.3	1.6–2.5
Unemployment rate	4.5	4.6	4.6	4.0	4.0–4.7	4.3–4.9	4.3–4.8	3.8–4.3	3.9–4.8	4.0–5.2	3.8–4.9	3.5–4.7
December projection	4.6	4.6	4.5	4.0	4.4–4.7	4.3–4.8	4.0–4.7	3.8–4.3	4.0–5.3	4.0–5.0	3.8–4.8	3.5–4.8
PCE inflation	3.3	2.5	2.1	2.0	3.0–3.8	2.2–2.8	2.0–2.2	2.0	2.8–4.1	2.0–3.5	2.0–3.0	2.0
December projection	3.1	2.5	2.1	2.0	2.9–3.5	2.3–2.7	2.0–2.2	2.0	2.6–4.1	2.2–3.5	2.0–3.0	2.0
Core PCE inflation[4]	3.6	2.6	2.1		3.5–3.9	2.3–2.8	2.0–2.2		3.5–4.1	2.1–3.1	2.0–3.0	
December projection	3.5	2.5	2.1		3.2–3.7	2.3–2.7	2.0–2.2		3.0–3.8	2.2–3.0	2.0–3.0	
Memo: Projected appropriate policy path												
Federal funds rate	5.1	4.3	3.1	2.5	5.1–5.6	3.9–5.1	2.9–3.9	2.4–2.6	4.9–5.9	3.4–5.6	2.4–5.6	2.3–3.6
December projection	5.1	4.1	3.1	2.5	5.1–5.4	3.9–4.9	2.6–3.9	2.3–2.5	4.9–5.6	3.1–5.6	2.4–5.6	2.3–3.3

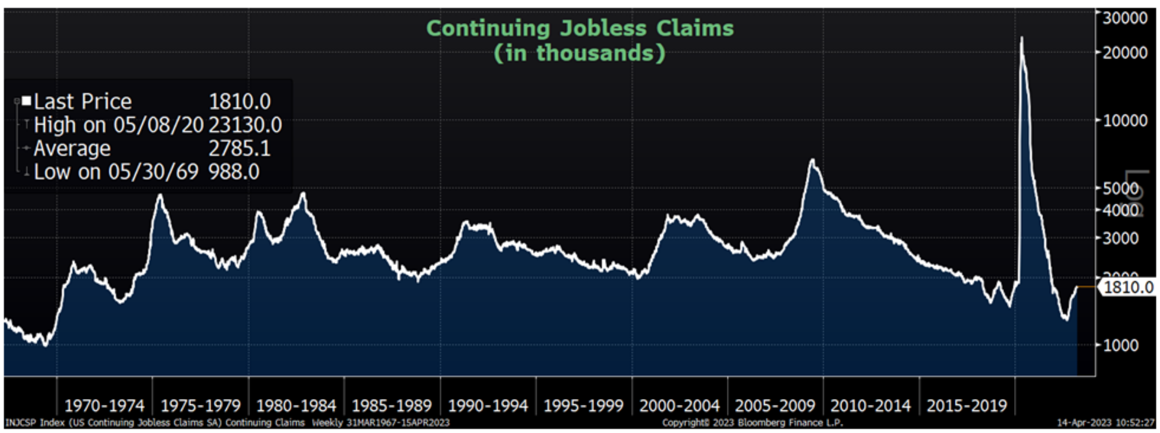
True, *Bloomberg* calculates that the chance of recession in the next 12 months stands at 65% today,…

…with the latest read on retail sales for March coming in below expectations with a 1.0% decline,…

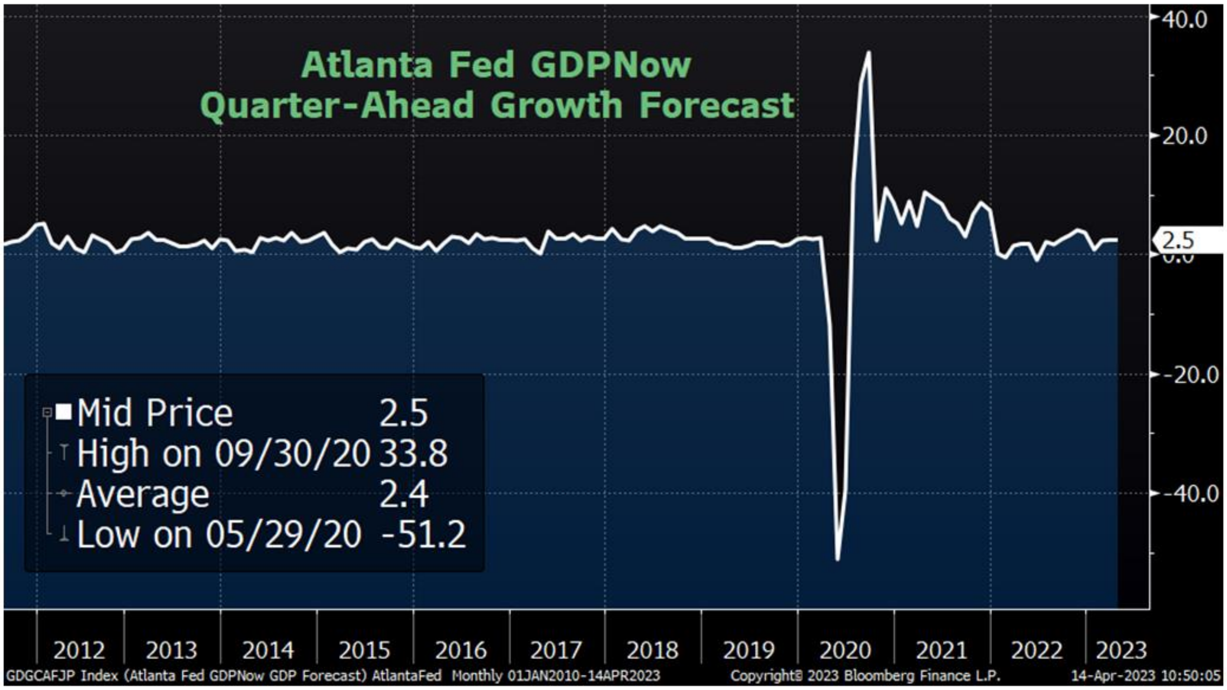


…and the number of first time filings for jobless benefits and continuing jobless claims now residing at higher levels than seen in recent months.



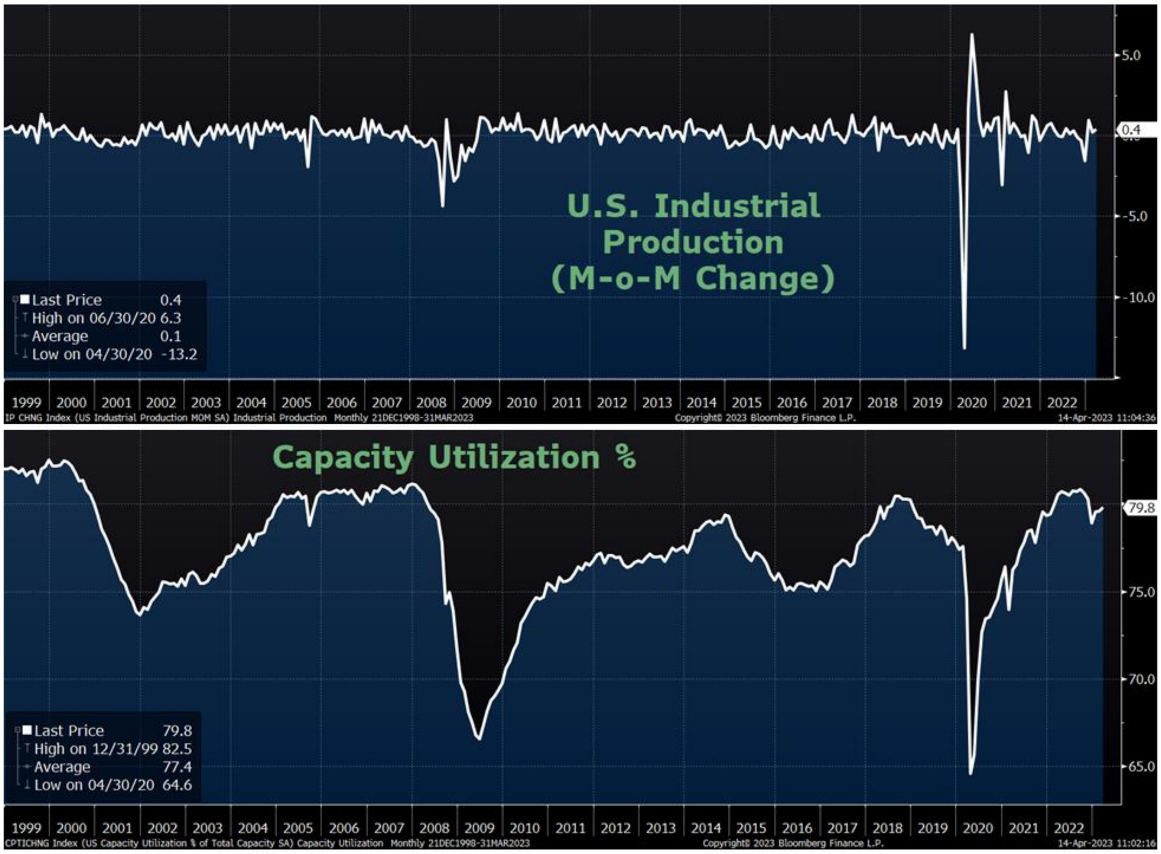


On the other hand, the latest projection from the Atlanta Fed for Q1 U.S. GDP growth rose to 2.5% last week, up from 1.5% a week ago…

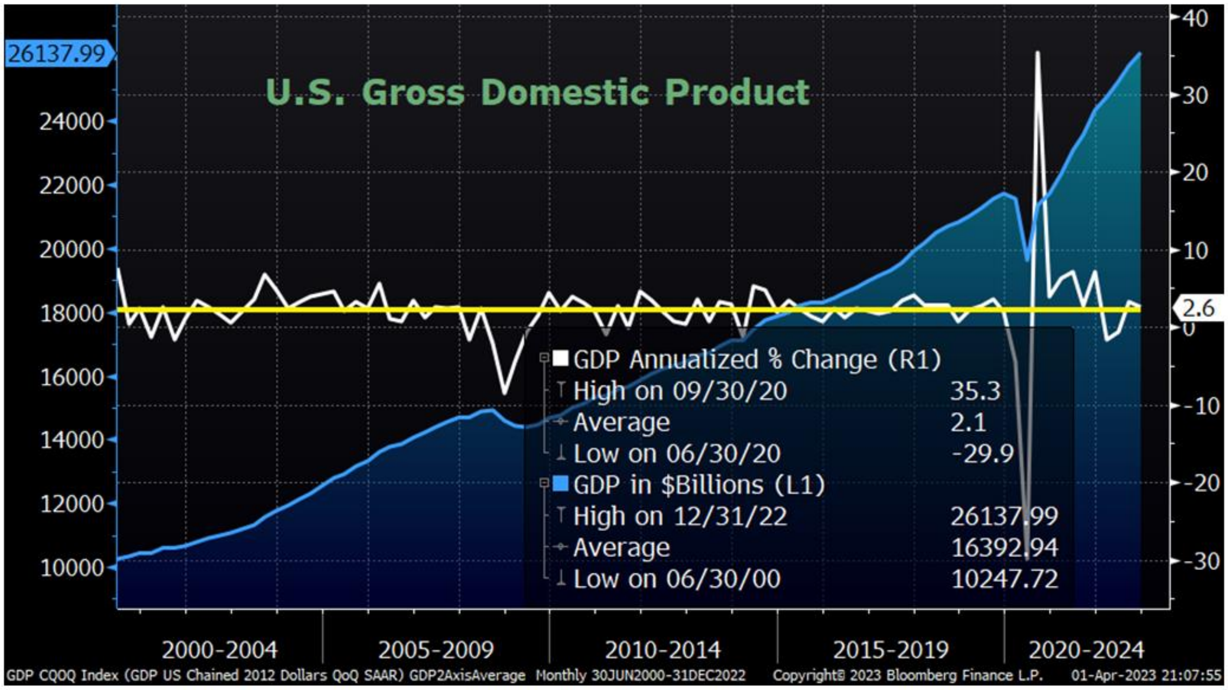


…as the mood of small business owners and folks on Main Street both came in better than expected, even as the respective figures were hardly anything to write home about,…

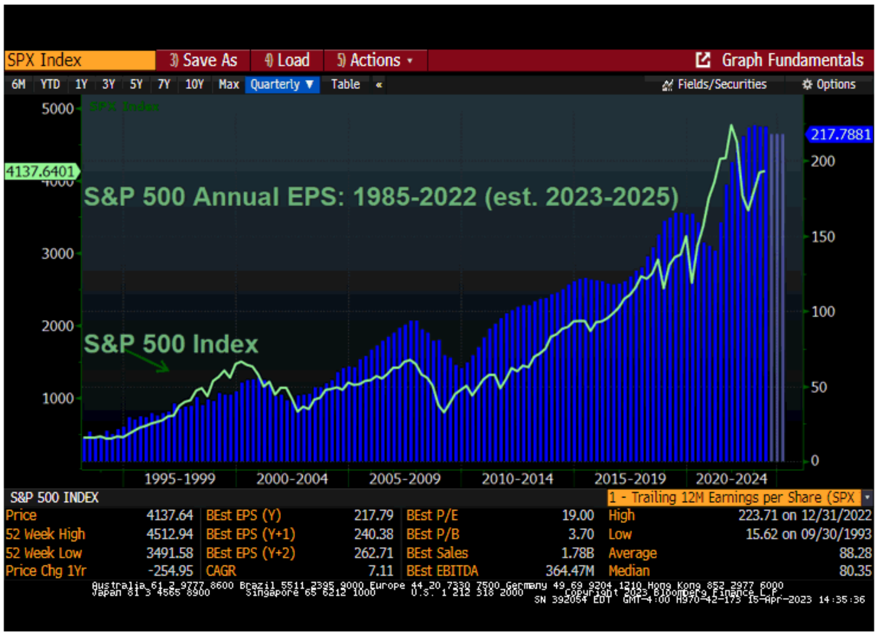
….and tallies for industrial production and capacity utilization topped estimates,…



…suggesting to us that the economy is likely to hold up reasonably well, especially on a nominal basis,…



…which should provide support for corporate profits, even if current analyst estimates likely are a bit too rosy.



S&P 500 Earnings Per Share		
Quarter Ended	Bottom Up Operating EPS 3 Month	Bottom Up Operating EPS 12 Month
ESTIMATES		
12/31/2024	$65.04	$244.52
9/30/2024	$62.90	$237.23
6/30/2024	$59.92	$230.65
3/31/2024	$56.66	$224.40
12/31/2023	$57.75	$217.77
9/30/2023	$56.32	$210.39
6/30/2023	$53.67	$204.42
3/31/2023	$50.03	$197.62
ACTUAL		
12/31/2022	$50.37	$196.95
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

Source: Standard & Poor's. As of 4.6.23

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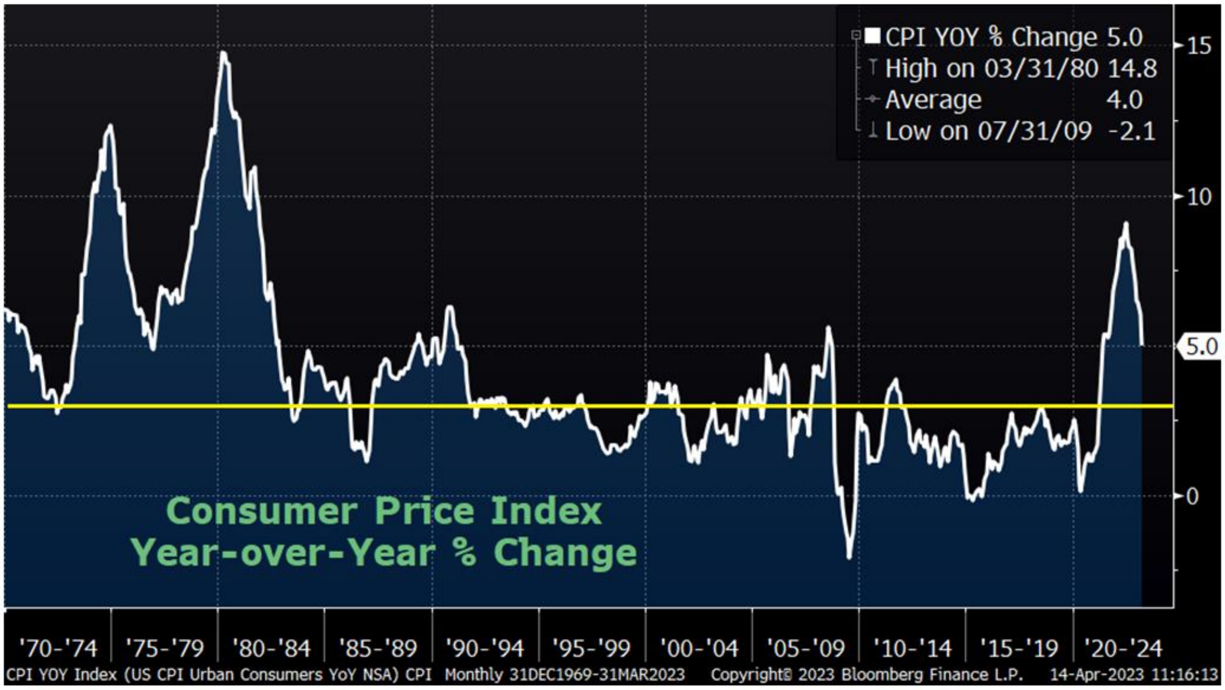
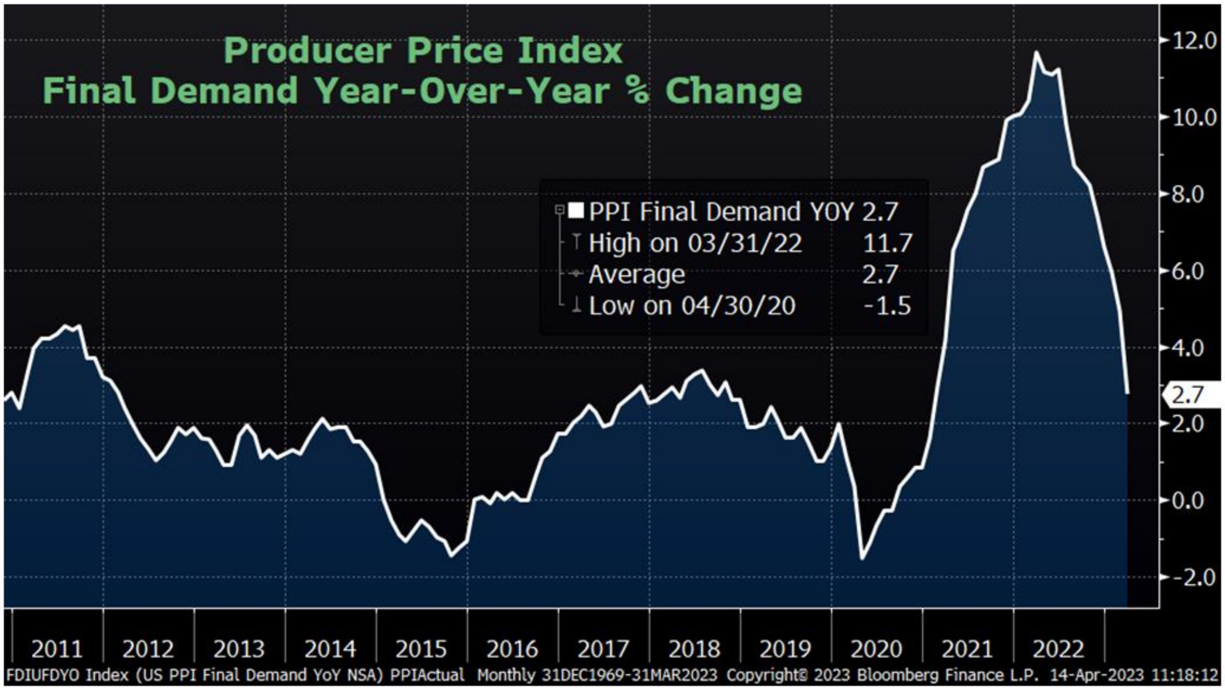
The most important of the economic numbers out last week were those related to inflation. Happily, both the consumer price index, which rose "only" 5.0% on a year-over-year basis in March, down from a 6.0% jump the month prior,…

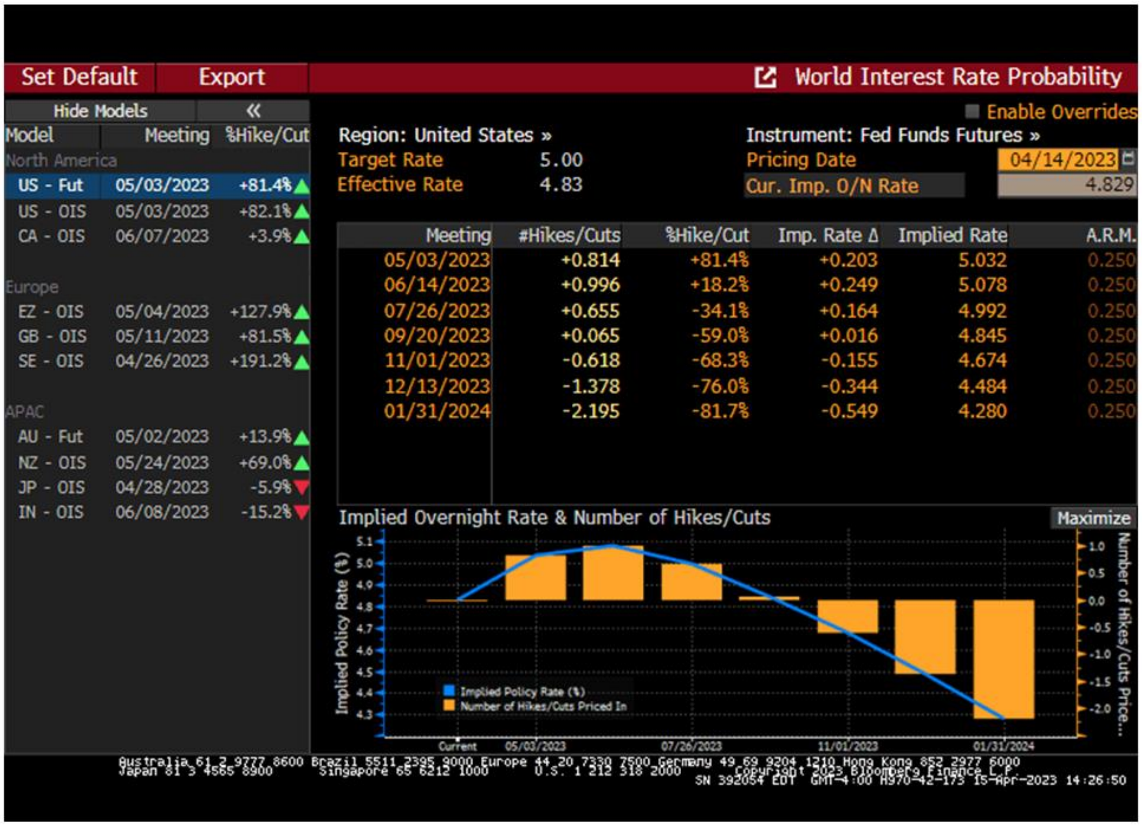


…and the producer price index, which increased 2.7% in March, versus a 4.9% rise in February,…



…suggest that the Fed is making some progress on the inflation front, even as San Francisco Fed President Mary Daly said on Wednesday, "While the full impact of this policy tightening is still making its way through the system, the strength of the economy and the elevated readings on inflation suggest that there is more work to do."

Market expectations for additional Federal Reserve rate hikes ticked higher last week, with the futures now pricing in a 5.08% peak in the Fed Funds rate this year and a year-end level of 4.48%. Those numbers compare to a 5.00% high and a 4.26% end-of-year figure indicated by the futures the week prior,…



…with the higher-for-longer shift in interest-rate sentiment contributing to a bump up in the yield last week on the benchmark 10-Year U.S. Treasury,…

…even as longer-term inflation expectations remain fairly contained.

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Obviously, the health of the economy remains a big question mark, but we continue to like the long-term prospects of 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	11.9	12.1	0.8	2.2	3.0
ValuePlus	12.7	12.5	1.1	2.3	2.5
Dividend Income	11.9	12.3	0.7	2.1	3.4
Focused Dividend Income	12.6	12.6	1.0	2.5	3.0
Focused ValuePlus	13.1	13.2	1.2	2.8	2.7
Small-Mid Dividend Value	10.2	10.1	0.5	1.5	3.1
Russell 3000	21.0	19.4	2.1	3.7	NA
Russell 3000 Growth	29.3	25.3	3.3	9.2	NA
Russell 3000 Value	16.1	15.6	1.5	2.3	NA
Russell 1000	20.6	19.2	2.3	4.0	NA
Russell 1000 Growth	28.7	25.0	3.6	10.0	NA
Russell 1000 Value	15.9	15.4	1.6	2.4	NA
S&P 500 Index	20.2	19.0	2.4	4.1	NA
S&P 500 Growth Index	20.3	20.6	3.3	7.1	NA
S&P 500 Value Index	19.6	17.0	1.8	2.8	NA
S&P 500 Pure Value Index	9.9	9.9	0.6	1.5	NA

As of 04.14.23. 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.

…and we take comfort in what market history has to say about recessions and the performance of Value Stocks and Dividend Payers, like those that we have long championed.

THE PRUDENT SPECULATOR

Modest equity losses could be avoided if one knew in advance when a recession officially began and when it ended, but unless one's timing was perfect, it is likely that a trader would be sitting on the sidelines before and after an economic contraction, missing out on sizable rewards.

Recession Start Date	Recession End Date	One Year Prior Value	One year Prior Div Payers	Return During Value	Return During Div Payers	One Year Post Value	One Year Post Div Payers	Five Years Post Value	Five Years Post Div Payers
08.31.1929	03.31.1933	30.9%	44.4%	-81.0%	-77.8%	205.5%	101.9%	123.3%	99.3%
05.31.1937	06.30.1938	42.0%	14.3%	-43.1%	-21.5%	-14.5%	2.1%	128.7%	58.2%
02.28.1945	10.31.1945	54.5%	30.0%	25.6%	20.0%	-2.3%	-4.5%	75.7%	58.1%
11.30.1948	10.31.1949	4.8%	2.4%	11.4%	15.7%	43.4%	31.2%	174.6%	153.9%
07.31.1953	05.31.1954	4.7%	3.0%	13.6%	22.8%	60.2%	38.1%	200.7%	151.2%
08.31.1957	04.30.1958	-0.4%	-1.0%	-2.0%	-0.2%	61.1%	42.7%	129.3%	102.3%
04.30.1960	02.28.1961	-6.4%	-2.5%	21.5%	21.5%	16.9%	14.6%	136.8%	73.7%
12.31.1969	11.30.1970	-20.9%	-10.9%	1.1%	-2.3%	11.1%	12.5%	44.1%	28.7%
11.30.1973	03.31.1975	-19.3%	-17.5%	13.0%	-3.3%	51.7%	31.4%	156.1%	76.4%
01.31.1980	07.31.1980	30.5%	24.0%	3.5%	8.7%	23.2%	16.4%	207.3%	109.4%
07.31.1981	11.30.1982	23.2%	16.4%	33.1%	15.7%	39.5%	25.6%	122.8%	99.8%
07.31.1990	03.31.1991	-7.3%	4.2%	5.1%	8.6%	25.6%	13.4%	150.6%	102.1%
03.31.2001	11.30.2001	22.3%	7.9%	3.7%	0.5%	-11.6%	-10.1%	93.4%	47.3%
12.31.2007	06.30.2009	-7.9%	4.9%	-39.2%	-34.4%	24.5%	14.2%	156.5%	136.5%
02.29.2020	04.30.2020	-9.7%	5.6%	-16.9%	-3.4%	85.8%	47.0%	N/A	N/A
	AVERAGE	**9.4%**	**8.4%**	**-3.4%**	**-2.0%**	**41.3%**	**25.1%**	**126.7%**	**86.5%**

Returns are not annualized. SOURCE: Kovitz using data from Bloomberg Finance L.P and Professors Fama and French

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 a several of our recommendations.

After the close of trading on Friday April 7, Samsung Electronics said it would make a "meaningful" cut to chip production, following the lead of smaller rivals, as it grapples with a downturn in semiconductor demand that has sent prices falling.

This output cut by the world's biggest memory chipmaker (accounting for half of the global DRAM market), was somewhat unusual and came on the heels of a worse-than-expected plunge in its first-quarter profit.

Smartphone and personal computer makers had stocked up on chips during the pandemic when demand for consumer devices skyrocketed, but manufacturers have been running down inventories as they try to better balance supply and demand.

Samsung did not disclose the size of the planned production reduction, but it sent a strong signal for a company that had previously said it would make small adjustments like pauses for refurbishing production lines but not a full-blown cut.

The fact that the number one market share firm is joining production cuts along with SK Hynix and **Micron** (MU – $62.63), has seemingly shifted the mindset of analysts and investors who are now looking for a memory chip rebound in the second half of the year. Shares of Micron have rallied almost 10% since the Samsung announcement, and are now up more than 25% in 2023.

Micron specializes in DRAM, the type of memory commonly used in PCs and data centers, and in NAND chips, which are the flash memory chips used in smaller devices like smartphones and USB drives.

Reports out this past week said memory chip prices staged a rebound for the first time in more than a year following the Samsung news, boosting hopes for a sooner-than-expected market recovery.

Like others, we believe the cuts to both capex and production by the three DRAM providers could speed up the timeframe of a DRAM recovery, especially considering PC demand (roughly 10% of DRAM) appears to have begun to stabilize and it is widely expected that both data center demand (roughly 40% of DRAM) and handset demand (roughly 30% of DRAM) will stabilize in the second half of the year. With the new information at hand, we have bumped up our Target Price for MU to $80.

Despite trading as high as $34 early in the week, shares of **Greenbrier Cos.** (GBX – $29.40) gave back some of their recent gain last week, falling over 2.5% over the five trading days. The retreat came even as the railcar maker reported Q2 financial results in line with what it released preliminarily at the end of March. The $0.99 per share earned in the quarter is more than double the figure a year ago as higher manufacturing volumes from record deliveries (7,600 units) lifted margins.

Greenbrier also held its *Investor Day* last Wednesday where it discussed its latest strategic plan. Management expressed that growing the leasing business was a priority as it endeavors to more than double recurring revenue in the next five years.

CEO Lorie Tekorius said, “Growing our fleet will accomplish several important strategic goals for Greenbrier. First, it’s going to drive volume to each of our business units: manufacturing, leasing and services and our maintenance services business. Second, it’s going to increase the stability of our earnings. Third, it’s going to allow us to enjoy significant tax benefits, which will reduce cash taxes and improve liquidity. And finally, it provides us an ownership and long-lived assets that we can remarket to new lessees or sell to other asset owners. And this generates additional revenue as we participate in the full cycle benefits that emerged from freight railcar economics."

The proof will be in the pudding, but we find the stock attractively priced at just 12 times NTM EPS estimates. Following a challenging prior year for those with a heavy manufacturing footprint, Greenbrier is positioned well to potentially benefit from an elevated focus on rail safety. We also like the 3.7% dividend yield. Our Target Price for GBX has been bumped up to $52.

Shares of **BlackRock** (BLK – $691.33) rallied more than 5% last week, with the lion's share of the advance coming on Friday after the investment management firm reported Q1 bottom-line results that were better than the consensus analyst estimates. BLK posted revenue of $4.24 billion, in line with the average forecast, while adjusted EPS came in at $7.93, versus the $7.67 projection. The quarter included $103 billion of long-term net inflows, driven by continued momentum in bond ETFs and significant client outsourcing mandates.

CEO Laurence D. Fink shared thoughts on the quarter:

BlackRock is helping clients execute on opportunities arising during this period of transition, driving $110 billion of total net inflows and positive annualized organic base fee growth in the first quarter. BlackRock is a source of both stability and optimism for clients. We are helping clients navigate volatility and embed resiliency in their portfolios, while also providing insights on the long-term opportunities to be had in today's markets."

BlackRock led the industry with $34 billion of bond ETF net inflows and accounted for over 60% of total fixed income ETF trading volume during the quarter. BlackRock ETFs once again proved their value as critically important tools for active management and in providing liquidity and transparency to clients. Aladdin continued to provide best-in-class portfolio and risk analytics, enabling clients to act quickly and with clarity and confidence. And clients turned to our $683 billion cash management platform to manage risk, diversify, and enhance yields.

BlackRock was founded on the belief that the capital markets would steadily grow as people, companies and countries turn to them to fund their retirements, businesses, and economies. I believe today's crisis of confidence in the regional banking sector will further accelerate capital markets growth, and BlackRock will be a central player. Increased financing through the capital markets will require the scale, multi-asset capabilities and excellence in portfolio construction that BlackRock consistently delivers across market cycles.

Throughout our history, moments of market dislocation and disruption have served as inflection points for BlackRock. We've always emerged stronger, more differentiated and more deeply connected with clients. We will continue to stay in front of client needs and execute on opportunities to deliver long-term growth for our clients, shareholders and employees.

Also of interest, in an on-set interview on *CNBC* Friday, Mr. Fink said he still thinks its quite plausible that the U.S. economy will avoid a recession all together, or it will be a shallow one. Why? "We have three giant fiscal stimuluses that were created in the last two years that are starting to enter our economy and that's the infrastructure bill, that's the chips act and the IRA, the cumulative impact of those three bills is a trillion dollars of stimulus over the next few years. Think about how many jobs infrastructure creates, think about the demand for commodities as we build infrastructure. So yes we have some sectors of the economy are starting to weaken, but we are going to have other segments of the economy, because of these tremendous fiscal stimuluses are going to offset some of that…and that's just beginning."

We continue to like that BlackRock's diversified investment & technology platform has demonstrated an all-weather track record of generating positive organic growth across good and bad times. This is driven by its broad suite of secular growth products where BLK is a leader or first-mover, including ETFs, technology solutions, ESG, outsourced solutions, retirement and alternative investments. BLK carries a current dividend yield of 2.9% and the company continues to buy back shares. Our Target Price has been boosted to $880.

Fears of tightening credit seemingly kept a lid on bank stocks on Friday as the KBW Banking index gained just 1.1%, carried by a 7.6% jump for shares of **JPMorgan Chase** (JPM – $138.73). This is despite earnings releases that morning from some of America's largest banks that beat their respective consensus estimates.

PNC Financial (PNC – $121.85) eked out a slight gain after spending much of the day in the red. Of course, shares of the regional bank remain 30% lower over the past year. PNC earned $3.98 per share in the latest quarter, a gain both year over year and quarter over quarter. Loans and deposits both grew modestly versus the prior quarter, efficiency and operating leverage improved, and charge-offs declined.

PNC's CFO Robert Reilly took care to provide detail related to several issues affecting regional banks today like their deposit base and the impact of security valuations on balance sheet equity. He also addressed commercial credit quality (office lending in particular), a segment for which credit has noticeably tightened this year.

At the end of the first quarter our deposits were 53% consumer and 47% commercial. Inside of our $230 billion of consumer deposits, approximately 90% are FDIC insured. The portfolio is very granular with an average account balance of approximately $11,500 across nearly 20 million accounts throughout our Coast-to-Coast franchise. Our $207 billion of commercial deposits are 20% insured, but importantly, approximately 95% of the total balance are held in operating and relationship accounts.

In light of the current environment, we anticipate that we will be subject to a total loss absorbing capacity requirement in some form and at some point, with a reasonable phase-in period. Importantly, as our borrowed funds continue to return to a more normalized level, we would expect to be compliant through our current issuance plans under existing TLAC requirements…As a Category III institution, we don't include AOCI in our CET1 ratio [9.2% at quarter end], but understand why there is focus on this ratio with the inclusion of AOCI. As of March 31, 2023, our CET1 ratio including AOCI was estimated to be 7.5%, which remains above our 7.4% required level, taking into account our current stress capital buffer…While AOCI takes into account the current valuation of the securities and certain portions of our swap *portfolios, it does not account for the valuation of the deposit book, which can be a meaningful offset in a rising interest rate environment. In fact, looking at PNC's change in market value of equity over the past year, the increase in the market value of our deposits in the rapidly rising interest rate environment has significantly outpaced all unrealized losses on the asset side of the balance sheet, including securities and fixed rate loans.*

While credit quality is strong across the majority of our CRE book, office is a segment receiving a lot of attention in this environment due to the shift to remote work and higher interest rates…The office portfolio was originated with an approximate loan to value of 55% to 60% and a significant majority of those properties are defined as Class A…To appropriately sensitize our portfolio, we significantly discounted net operating income levels and property values across the entire office book…Additionally, tenant retention, build-out costs and concession levels are all updated to accurately reflect market conditions. Credit quality in our office portfolio remains strong today with only 0.2% of loans delinquent, 3.5% nonperforming and a net charge-off rate of 47 basis points over the last 12 months.

PNC appears well suited to weather the latest banking predicament given shorter-duration instruments on the balance sheet and a relatively small unrealized loss on its held-to-maturity securities compared to peers. Nevertheless, shares have skidded nearly 40% since the beginning of 2022 even as the company further expanded its reach via the acquisition of BBVA's U.S. retail operation in 2021. Shares trade for just 9 times the NTM EPS estimate and yield a whopping 4.9%, with a dividend coverage of more than 2X. Our Target Price for PNC is now $214.

International money-center investment bank **Citigroup** (C – $49.56) earned $1.86 per share (vs. $1.65 est.) on strong fixed income, currency & commodity trading. Revenue increased 12% year-over-year to $21.5 billion (6% excluding divestiture-related impacts) as growth in net-interest income from higher interest rates was partially offset by lower non-interest revenues.

CEO Jane Fraser said, "Citi delivered strong operating performance, showing good revenue growth and expense discipline despite the tumultuous environment for banks. Our robust and well-managed balance sheet was a source of strength for our clients, and we continue making progress in executing our strategy focused on our five core interconnected businesses while simplifying and transforming the firm. [Treasury and Trading Solutions] continued to perform extremely well, growing non-interest revenue on new mandates and strong cross-border activity. Markets saw the third best quarter in the last decade in Fixed Income. Banking activity picked up from the end of 2022. Our two cards businesses are showing momentum. While it is not an ideal environment for wealth management, the drivers of this business continue to be very positive, and we announced that Andy Sieg will be joining us as its CEO later this year."

She concluded, "We closed the sale of two consumer franchises, which contributed to our healthy pace of capital generation. We ended the quarter with a CET1 ratio of 13.4%. We are committed to increasing the amount of excess capital we return over time as well as delivering with excellence for our clients and shareholders."

Our patience is not infinite, but we continue to believe in the turnaround effort at Citi under Ms. Fraser. We appreciate Citi's leverage to the U.S. economy along with its potential to show outsized benefits from its businesses abroad, thanks to its unique exposure to worldwide card loan growth, global transactions and trade volumes. C shares, which are priced at half of book value and for around 8 times NTM EPS estimates, yield 4.1%. Our Target Price for C has been raised to $79.

Jamie Dimon & Company produced another solid Q1, beating the Street's consensus estimates on most counts, including both fee and net interest income (margin), efficiency and credit quality ($1.1 billion of net charge-offs vs. $1.2 billion est.). JPM earned its highest quarterly profit in two years of $4.10 per share on strong net interest income and trading revenues.

The financial titan also lifted its net interest income forecast for 2023 to approximately $81 billion, a function of lower deposit rate-paid assumptions across both consumer and wholesale based on the market's expectation of Fed cuts later in the year in tandem with slightly higher card revolving balances. This forecast is also at the high end of management's average market cycle expectation of around $70 billion.

We continue to appreciate the fortress balance sheet at JPMorgan as well as its ability to generate profits in varied environments. After the latest bump, shares still trade for about 11 times the lowest analyst EPS estimate for 2023 and yield 2.9%. Our Target Price for JPM has been raised to $183.