

# Market Commentary Monday, January 27, 2020

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## EXECUTIVE SUMMARY

Week in Review – Stocks End with a Thud

Wuhan Coronavirus – Global Worry Rising

Viral Perspective – Influenza Killed 34,000 Americans Last Year

Volatility – Stock Prices Will Gyrate and 5% and 10% Declines are not Unusual

Viral History Part 1 – Ebola 2014 Commentary

Viral History Part 2 – Despite some 800 SARS-Related Deaths, 2003 Was a Very Good Year for Stocks

Econ Outlook – Subdued Global Growth Expected

Stocks vs. Bonds – Falling Yields Add to the Appeal of Equities

2020 Laggards – 25 Undervalued Purchase Candidates

*Fewer, Richer, Greener* – New Book Offers Food for Long-Term Thought

Stock News – Updates on JNJ, ABT, COF, IBM, CMCSA, INTC, LRCX, COHU, KLIC, KEY, CMA, FITB, SYF & ONB

## Market Review

It was a lousy end to a not-so-grand holiday-shortened trading week, in which the major market averages dropped 1% or so and the average stock in the Russell 3000 gave up all its January gains to now be down 0.5% thus far in 2020. Interestingly, the big skid on Friday was not supposed to happen, if the URL for the *Market Snapshot* story that the *MarketWatch* website was running was to be believed: [https://www.marketwatch.com/story/dow-seen-opening-in-positive-territory-as-intel-amex-shares-punch-higher-in-premarket-action-2020-01-24?mod=mw\\_latestnews](https://www.marketwatch.com/story/dow-seen-opening-in-positive-territory-as-intel-amex-shares-punch-higher-in-premarket-action-2020-01-24?mod=mw_latestnews).

Of course, the *MarketWatch* folks didn't bother to change the upbeat URL language, even as when folks click on that link today, they are greeted with the headline, "Stocks slide to lowest level in over a week as spread of China virus worries investors." Indeed, conditions changed rapidly, with Wuhan coronavirus fears pushing the Trump Impeachment Proceedings down the page of the various news websites, before the tragic death of basketball superstar Kobe Bryant, his daughter, and apparently 7 others, became a massive Breaking News story on Sunday.

No doubt, coronavirus developments are of major import to investors as the new trading week begins, with the U.S. equity futures selling off sharply as these comments were penned on Sunday evening. CNN.com's latest update included news that more than 50 confirmed cases have been identified in 13 places outside mainland China and that more than 60 million people have been affected by Beijing's attempts to either partially or fully lock down affected cities. Further, President Xi Jinping said that China is facing a "grave situation" and, "Life is of

paramount importance. When an epidemic breaks out, a command is issued. It is our responsibility to prevent and control it.” And, China’s health minister said that people can spread the virus before symptoms show, which makes it harder to contain.

Clearly, the coronavirus situation is scary, especially as there now is a confirmed case in our home county of Orange County, California, but we always try to put frightening events into perspective, especially as we live today in such a sensationalistic society, with viral, no pun intended, social media and Internet posts constantly bombarding the senses.

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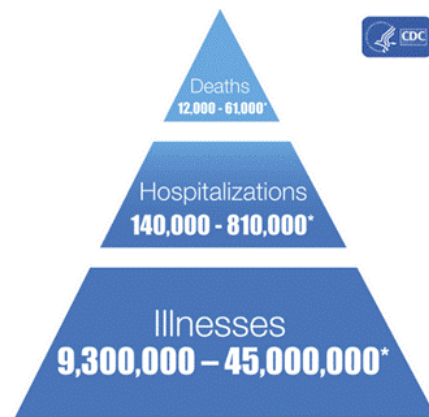
**THE PRUDENT SPECULATOR**  
Perspective: 34K U.S. Flu Deaths Last Year

While the Wuhan coronavirus is certainly a concern to global health and wealth, it is interesting to compare the most recent statistics of at least 2700 confirmed cases and at least 80 deaths, the latter all in China, along with 5 people supposedly showing symptoms in the U.S., including one in Orange County, California, to the annual U.S. Influenza numbers.

**U.S. Influenza Disease Burden, by Season**

Season	Symptomatic Illnesses Estimate	Medical Visits Estimate	Hospitalizations Estimate	Deaths Estimate
2010-2011	21,000,000	10,000,000	290,000	37,000
2011-2012	9,300,000	4,300,000	140,000	12,000
2012-2013	34,000,000	16,000,000	570,000	43,000
2013-2014	30,000,000	13,000,000	350,000	38,000
2014-2015	30,000,000	14,000,000	590,000	51,000
2015-2016	24,000,000	11,000,000	280,000	23,000
2016-2017	29,000,000	14,000,000	500,000	38,000
2017-2018	45,000,000	21,000,000	810,000	61,000
2018-2019	35,520,883	16,520,350	490,561	34,157

Source: Center for Disease Control & Prevention: <https://www.cdc.gov/flu/about/burden/index.html>



\*The top range of these burden estimates are from the 2017-2018 flu season. These are preliminary and may change as data are finalized.

To be sure, Wuhan coronavirus could be the catalyst for the next 5% market pullback,...



# THE PRUDENT SPECULATOR

## Ups and Downs Aplenty...Just Since '09

**S&P 500 Moves (on a Closing Basis) of 5% Without a Comparable Move in the Opposite Direction**

2/9/2009	3/9/2009	-22.23%	BEAR	3/9/2009	3/26/2009	23.11%	BULL
3/26/2009	3/30/2009	-5.44%	BEAR	3/30/2009	6/12/2009	20.15%	BULL
6/12/2009	7/10/2009	-7.09%	BEAR	7/10/2009	10/19/2009	24.89%	BULL
10/19/2009	10/30/2009	-5.62%	BEAR	10/30/2009	1/19/2010	11.01%	BULL
1/19/2010	2/8/2010	-8.13%	BEAR	2/8/2010	4/23/2010	15.19%	BULL
4/23/2010	5/7/2010	-8.74%	BEAR	5/7/2010	5/12/2010	5.47%	BULL
5/12/2010	6/7/2010	-10.34%	BEAR	6/7/2010	6/18/2010	6.38%	BULL
6/18/2010	7/2/2010	-8.49%	BEAR	7/2/2010	8/9/2010	10.29%	BULL
8/9/2010	8/26/2010	-7.14%	BEAR	8/26/2010	2/18/2011	28.25%	BULL
2/18/2011	3/16/2011	-6.41%	BEAR	3/16/2011	4/29/2011	8.49%	BULL
4/29/2011	6/15/2011	-7.20%	BEAR	6/15/2011	7/7/2011	6.94%	BULL
7/7/2011	8/8/2011	-17.27%	BEAR	8/8/2011	8/15/2011	7.60%	BULL
8/15/2011	8/19/2011	-6.72%	BEAR	8/19/2011	8/31/2011	8.49%	BULL
8/31/2011	9/9/2011	-5.30%	BEAR	9/9/2011	9/16/2011	5.35%	BULL
9/16/2011	10/3/2011	-9.60%	BEAR	10/3/2011	10/28/2011	16.91%	BULL
10/28/2011	11/25/2011	-9.84%	BEAR	11/25/2011	4/2/2012	22.47%	BULL
4/2/2012	6/1/2012	-9.94%	BEAR	6/1/2012	9/14/2012	14.69%	BULL
9/14/2012	11/15/2012	-7.67%	BEAR	11/15/2012	5/21/2013	23.34%	BULL
5/21/2013	6/24/2013	-5.76%	BEAR	6/24/2013	1/15/2014	17.50%	BULL
1/15/2014	2/3/2014	-5.76%	BEAR	2/3/2014	9/18/2014	15.47%	BULL
9/18/2014	10/15/2014	-7.40%	BEAR	10/15/2014	3/2/2015	13.69%	BULL
5/21/2015	8/25/2015	-12.35%	BEAR	8/25/2015	9/16/2015	6.84%	BULL
9/16/2015	9/28/2015	-5.69%	BEAR	9/28/2015	11/3/2015	12.12%	BULL
11/3/2015	2/11/2016	-13.31%	BEAR	2/11/2016	6/23/2016	5.64%	BULL
6/23/2016	6/27/2016	-5.34%	BEAR	6/27/2016	1/26/2018	43.60%	BULL
1/26/2018	2/8/2018	-10.16%	BEAR	2/8/2018	3/9/2018	7.96%	BULL
3/9/2018	4/2/2018	-7.35%	BEAR	4/2/2018	9/20/2018	13.55%	BULL
9/20/2018	11/23/2018	-10.17%	BEAR	11/23/2018	12/3/2018	5.99%	BULL
12/3/2018	12/24/2018	-15.74%	BEAR	12/24/2018	4/30/2019	25.30%	BULL
4/30/2019	6/3/2019	-6.84%	BEAR	6/3/2019	7/24/2019	10.02%	BULL
7/24/2019	8/14/2019	-6.12%	BEAR	8/14/2019	1/17/2020	14.69%	BULL
<b>Average Drop</b>		<b>-8.88%</b>	<b>BEAR</b>	<b>Average Increase</b>		<b>14.56%</b>	<b>BULL</b>

While the S&P 500 skidded 6.8% during an ugly May 2019, and fell 6.1% from late-July to mid-August, few likely realize that these were the 29<sup>th</sup> and 30<sup>th</sup> pullbacks of 5% or more without an intervening 5% recovery just since the Financial Crisis market low on March 9, 2009. Happily, the returns in the 30 periods where the S&P has gained more than 5% over the past 10+ years have dwarfed the losses.

...or even the next 10% correction,...



# THE PRUDENT SPECULATOR

## 10% Ups and Downs Since TPS Inception

**S&P 500 Moves (on a Closing Basis) of 10% Without a Comparable Move in the Opposite Direction**

9/12/1978	11/14/1978	-13.55%	BEAR	11/14/1978	10/5/1979	20.30%	BULL
10/5/1979	11/7/1979	-10.25%	BEAR	11/7/1979	2/13/1980	18.59%	BULL
2/13/1980	3/27/1980	-17.07%	BEAR	3/27/1980	11/28/1980	43.07%	BULL
11/28/1980	9/25/1981	-19.75%	BEAR	9/25/1981	11/30/1981	12.04%	BULL
11/30/1981	3/8/1982	-15.05%	BEAR	3/8/1982	5/7/1982	11.30%	BULL
5/7/1982	8/12/1982	-14.27%	BEAR	8/12/1982	10/10/1983	68.57%	BULL
10/10/1983	7/24/1984	-14.38%	BEAR	7/24/1984	8/25/1987	127.82%	BULL
8/25/1987	10/19/1987	-33.24%	BEAR	10/19/1987	10/21/1987	14.92%	BULL
10/21/1987	10/26/1987	-11.89%	BEAR	10/26/1987	11/2/1987	12.33%	BULL
11/2/1987	12/4/1987	-12.45%	BEAR	12/4/1987	10/9/1989	60.68%	BULL
10/9/1989	1/30/1990	-10.23%	BEAR	1/30/1990	7/16/1990	14.23%	BULL
7/16/1990	10/11/1990	-19.92%	BEAR	10/11/1990	10/7/1997	232.74%	BULL
10/7/1997	10/27/1997	-10.80%	BEAR	10/27/1997	7/17/1998	35.32%	BULL
7/17/1998	8/31/1998	-19.34%	BEAR	8/31/1998	9/23/1998	11.37%	BULL
9/23/1998	10/8/1998	-10.00%	BEAR	10/8/1998	7/16/1999	47.88%	BULL
7/16/1999	10/15/1999	-12.08%	BEAR	10/15/1999	3/24/2000	22.45%	BULL
3/24/2000	4/14/2000	-11.19%	BEAR	4/14/2000	9/1/2000	12.10%	BULL
9/1/2000	4/4/2001	-27.45%	BEAR	4/4/2001	5/21/2001	19.00%	BULL
5/21/2001	9/21/2001	-26.43%	BEAR	9/21/2001	1/4/2002	21.40%	BULL
1/4/2002	7/23/2002	-31.97%	BEAR	7/23/2002	8/22/2002	20.68%	BULL
8/22/2002	10/9/2002	-19.31%	BEAR	10/9/2002	11/27/2002	20.87%	BULL
11/27/2002	3/11/2003	-14.71%	BEAR	3/11/2003	10/9/2007	95.47%	BULL
10/9/2007	3/10/2008	-18.64%	BEAR	3/10/2008	5/19/2008	12.04%	BULL
5/19/2008	10/10/2008	-36.97%	BEAR	10/10/2008	10/13/2008	11.58%	BULL
10/13/2008	10/27/2008	-15.39%	BEAR	10/27/2008	11/4/2008	18.47%	BULL
11/4/2008	11/20/2008	-25.19%	BEAR	11/20/2008	1/6/2009	24.22%	BULL
1/6/2009	3/9/2009	-27.62%	BEAR	3/9/2009	4/23/2010	79.93%	BULL
4/23/2010	7/2/2010	-15.99%	BEAR	7/2/2010	4/29/2011	33.35%	BULL
4/29/2011	10/3/2011	-19.39%	BEAR	10/3/2011	5/21/2015	93.85%	BULL
5/21/2015	8/25/2015	-12.35%	BEAR	8/25/2015	11/3/2015	12.97%	BULL
11/3/2015	2/11/2016	-13.31%	BEAR	2/11/2016	1/26/2018	57.07%	BULL
1/26/2018	2/8/2018	-10.16%	BEAR	2/8/2018	9/20/2018	13.55%	BULL
9/20/2018	12/24/2018	-19.78%	BEAR	12/24/2018	1/17/2020	41.62%	BULL
<b>Average Drop</b>		<b>-17.88%</b>	<b>BEAR</b>	<b>Average Increase</b>		<b>40.66%</b>	<b>BULL</b>

While the S&P 500 skidded 19.8% during an ugly three-month period a year ago, we suspect that memories of corrections past have faded with stocks now at all-time highs. Believe it or not, there have been 33 pullbacks of 10% or more without an intervening 10% recovery since the launch of *The Prudent Speculator* more than 42 years ago. Happily, the returns in the winning periods have dwarfed the losses.

...but we think that this will eventually pass and that it will not be the virus that does humanity or stocks in. We do not mean to sound cavalier, but here is what we wrote back in 2014 as the equity markets were heading south in the wake of the Ebola scare...

*Of course, the frightening headlines surrounding Ebola and the lack of confidence most folks have in the government's ability to contain the virus did not help the cause. And yours truly had his own Ebola scare when informed by his sophomore daughter that one of two Yale graduate students who had just returned from conducting Ebola-related research in Liberia had been rushed "out of an abundance of caution" to the Yale-New Haven hospital with a low-grade fever, an early symptom of the dreaded disease. Reassurances from the powers-that-be that the students had no contact with Ebola patients or caregivers gave way to serious concerns when it was learned that the Yale actually came in direct contact on September 30 with NBC cameraman Ashoka Mupko, who was diagnosed with Ebola on Oct. 1. Happily, two Ebola tests have since come back negative and both of the students are now in quarantine, so the Yale case seems to be one of many false alarms.*

*Though Ebola news on the domestic front calmed a bit over the weekend, the death toll in West Africa continues to rise and we understand that it is nearly impossible to quarantine a continent. Obviously, we are a long way away from finding a cure for the disease and it would seem that U.S. healthcare officials are only beginning to get their arms around the treatment and*

containment protocols. Hard to imagine that developments related to Ebola won't get worse before they get better, but we do not think that there will be a long-term impact on the equity markets. After all, stocks have already survived HIV, SARS, Avian Flu, Swine Flu and a host of other ailments. Indeed, capitalism's immune system is quite strong.

We certainly do not wish to downplay the concerns related to Ebola, especially as Hollywood has done its part to suggest that a deadly virus may lead to the downfall of mankind (*The Andromeda Strain*, *I am Legend*, *Contagion* and *Planet of the Apes*, to name a few movies). However, in terms of the long-term impact on the equity markets, a review of previous significant epidemic/pandemics shows that stocks actually did quite well during the 1918-1919 influenza pandemic, the 1957-1958 Asian Flu, the 2002-2003 SARS scare and the 2009-2010 Swine Flu outbreak. Also, HIV, which has purportedly killed more than 30 million and counting, traces its start back to 1981, right near the beginning of the great Bull Market.

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**THE PRUDENT SPECULATOR**  
**Viruses Have Yet to Kill the Stock Market**



August 24, 2009



September 26, 2005



May 5, 2003



July 4, 1983

Interestingly, things did get worse before they got better back in 2014, with the S&P 500 bottoming around 1850 (today, the index is at 3295!) just a few days after your editor appeared on *Fox Business News*, offering the same message that would be repeated today, Keep Calm and Invest!

<https://video.foxbusiness.com/v/3837282711001/#sp=show-clips>

Obviously, the timing of the coronavirus outbreak could not have been worse, given all of the travel and activities planned around the Lunar New Year, so we realize that 2003 and the SARS outbreak is a better comparison than Ebola in 2014, given the size of the potential economic impact. Of course, from May 5, 2003, the *Time Magazine* SARS publication date shown above, through the end of that year, the S&P 500 returned 21.44% and the Russell 3000 Value index returned 25.25%!

That said, it is hard to imagine that global GDP growth won't be impacted, though it isn't as if the worldwide economy was expected to boom...



## THE PRUDENT SPECULATOR IMF: Tweaks to the Growth Projections

Global GDP growth, per the IMF, is now expected to increase from 2.9% in 2019 to 3.3% in 2020 and 3.4% in 2021.

Table 1. Overview of the World Economic Outlook Projections  
(Percent change, unless noted otherwise)

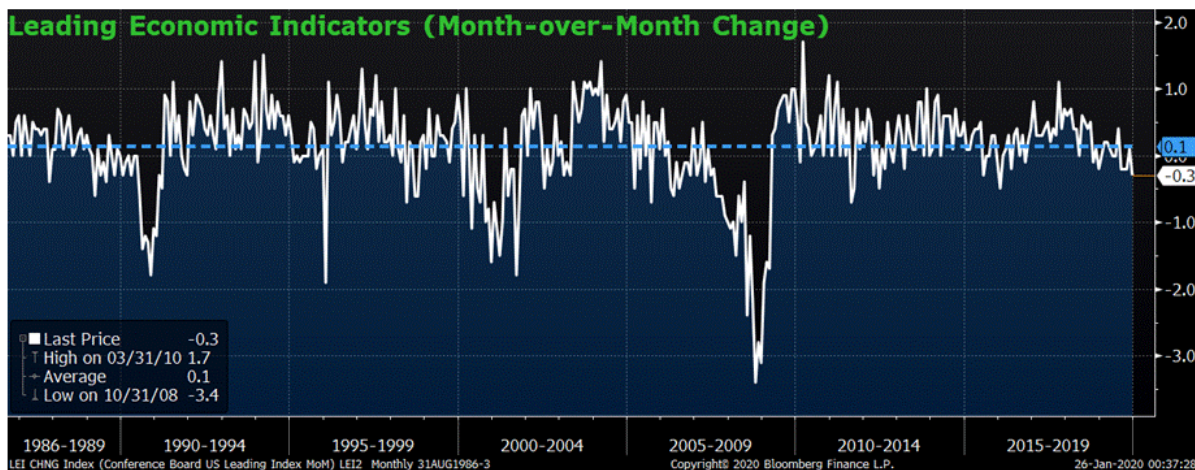
	Year over Year				Difference from Oct 2019 WEO Projections 1/	
	Estimate		Projections		2020	2021
	2018	2019	2020	2021		
<b>World Output</b>	<b>3.6</b>	<b>2.9</b>	<b>3.3</b>	<b>3.4</b>	<b>-0.1</b>	<b>-0.2</b>
<b>Advanced Economies</b>	<b>2.2</b>	<b>1.7</b>	<b>1.6</b>	<b>1.6</b>	<b>-0.1</b>	<b>0.0</b>
United States	2.9	2.3	2.0	1.7	-0.1	0.0
Euro Area	1.9	1.2	1.3	1.4	-0.1	0.0
Germany	1.5	0.5	1.1	1.4	-0.1	0.0
France	1.7	1.3	1.3	1.3	0.0	0.0
Italy	0.8	0.2	0.5	0.7	0.0	-0.1
Spain	2.4	2.0	1.6	1.6	-0.2	-0.1
Japan	0.3	1.0	0.7	0.5	0.2	0.0
United Kingdom	1.3	1.3	1.4	1.5	0.0	0.0
Canada	1.9	1.5	1.8	1.8	0.0	0.0
Other Advanced Economies 3/	2.6	1.5	1.9	2.4	-0.1	0.1
<b>Emerging Market and Developing Economies</b>	<b>4.5</b>	<b>3.7</b>	<b>4.4</b>	<b>4.6</b>	<b>-0.2</b>	<b>-0.2</b>
Emerging and Developing Asia	6.4	5.6	5.8	5.9	-0.2	-0.3
China	6.6	6.1	6.0	5.8	0.2	-0.1
India 4/	6.8	4.8	5.8	6.5	-1.2	-0.9
ASEAN-5 5/	5.2	4.7	4.8	5.1	-0.1	-0.1
Emerging and Developing Europe	3.1	1.8	2.6	2.5	0.1	0.0
Russia	2.3	1.1	1.9	2.0	0.0	0.0
Latin America and the Caribbean	1.1	0.1	1.6	2.3	-0.2	-0.1
Brazil	1.3	1.2	2.2	2.3	0.2	-0.1
Mexico	2.1	0.0	1.0	1.6	-0.3	-0.3
Middle East and Central Asia	1.9	0.8	2.8	3.2	-0.1	0.0
Saudi Arabia	2.4	0.2	1.9	2.2	-0.3	0.0
Sub-Saharan Africa	3.2	3.3	3.5	3.5	-0.1	-0.2
Nigeria	1.9	2.3	2.5	2.5	0.0	0.0
South Africa	0.8	0.4	0.8	1.0	-0.3	-0.4
Memorandum						
Low-Income Developing Countries	5.0	5.0	5.1	5.1	0.0	-0.1
World Growth Based on Market Exchange Rates	3.0	2.4	2.7	2.8	0.0	0.0

Source: International Monetary Fund (IMF) January 2020

While negative surprises to economic activity in a few emerging market economies, notably India, weighed, estimates were supported by “tentative signs that manufacturing activity and global trade are bottoming out, a broad-based shift toward accommodative monetary policy, intermittent favorable news on US-China trade negotiations, and diminished fears of a no-deal Brexit.”

...while the U.S. economy appears likely to see growth only in the 2% range this year.

The forward-looking index of Leading Economic Indicators was down 0.3% on a month-over-month basis in December. Rising unemployment insurance claims and a drop in housing permits weighed on the Conference Board's tally, but the keeper of the metric added that financial conditions and consumers' outlook for the economy remain positive, which should support growth of about 2% through early 2020.

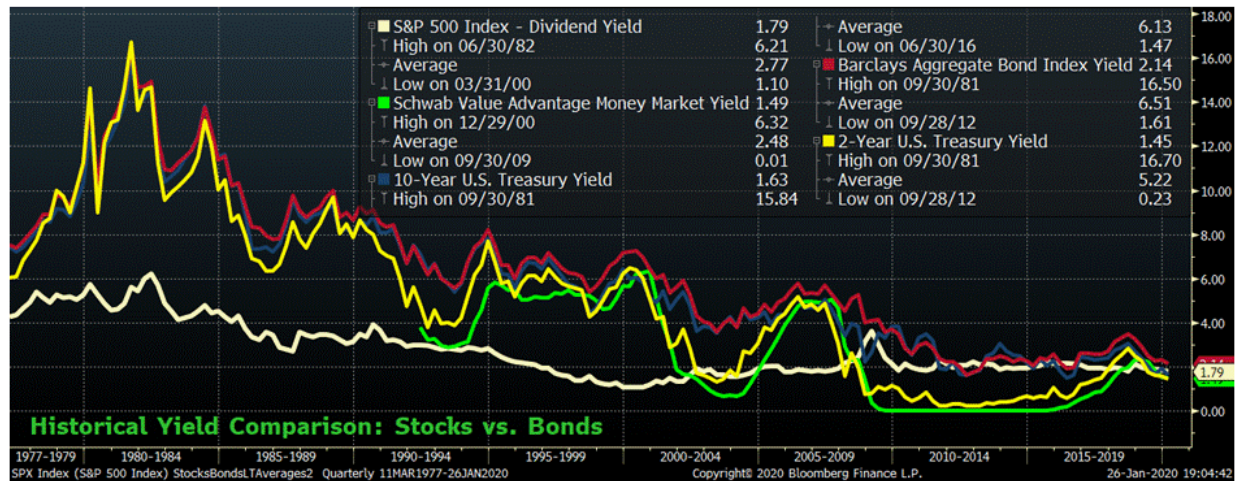


So, we do not think a ton of good news on the economic front has been priced into stocks, especially considering the historically low interest rate environment, whereby yields have just tumbled anew in the last few days.

# THE PRUDENT SPECULATOR

## Equity vs. Fixed Income Yields

Though stocks are not necessarily a substitute for bonds, U.S. Treasuries and money market funds, the current payout on the S&P 500 (1.79%) is still very generous versus the income provided by fixed income, especially given the recent plunge in rates. And, the comparisons to the average yields for all of the securities below very much favors equities.



Certainly, we are braced for a rocky trading week and we always understand that anything can happen in the stock market. Still, we see no reason to alter our enthusiasm for the long-term prospects of what we believe to be undervalued stocks in our broadly diversified portfolios. And, for those looking to take advantage of market turbulence, we note that the diversified list of stocks below is drawn from names that are down 5% or more this year.



Laggards Since the End of 2019														
Symbol	Common Stock	TR % Since 12.31.19	1.24.20 Price	Target Price	Sector	P/E	P/S	P/TBV	ROCE	EV/EBITDA	FCF Yld	Debt/TE (%)	Div Yld	Market Cap
AMGN	Amgen	-6.4	\$225.59	\$259.62	Pharma, Biotech	15.4	5.7	nmf	63.8	11.8	6.6	nmf	2.8%	134,042
AXAHY	AXA SA	-5.4	\$26.63	\$40.16	Insurance	9.9	nmf	nmf	2.3	nmf	nmf	nmf	4.6%	64,383
BASFY	BASF SE	-6.5	\$17.50	\$28.00	Materials	15.9	0.9	2.4	24.0	10.2	3.0	71%	3.7%	64,294
BIIB	Biogen	-6.3	\$278.14	\$452.87	Pharma, Biotech	8.6	3.5	10.3	38.9	6.6	11.9	100%	0.0%	50,188
BK	Bank of New York Mellon	-8.1	\$45.95	\$61.24	Diversified Financials	11.4	nmf	2.4	11.4	nmf	nmf	nmf	2.7%	41,386
CE	Celanese	-7.0	\$114.51	\$155.82	Materials	11.6	2.1	10.0	28.9	12.6	8.1	257%	2.2%	13,841
CMA	Comerica	-9.8	\$64.73	\$99.32	Banks	8.3	nmf	1.4	16.1	nmf	nmf	nmf	4.1%	9,331
CMI	Cummins	-5.5	\$169.15	\$200.36	Capital Goods	10.7	1.1	4.7	33.9	7.2	9.7	35%	3.1%	25,914
GBX	Greenbrier Cos	-21.9	\$25.34	\$42.86	Capital Goods	9.3	0.3	0.8	4.8	6.0	-22.6	83%	4.3%	826
GM	General Motors	-6.3	\$34.31	\$48.89	Automobiles & Components	5.5	0.3	1.3	21.2	2.1	21.6	181%	4.4%	49,022
GT	Goodyear Tire	-8.7	\$14.20	\$24.66	Automobiles & Components	10.1	0.2	0.8	4.0	5.7	1.3	150%	4.5%	3,309
HFC	HollyFrontier	-8.2	\$46.53	\$72.94	Energy	7.0	0.4	2.5	14.2	5.1	19.6	92%	3.0%	7,509
ING	ING Groep NV	-6.5	\$11.27	\$16.71	Banks	7.7	nmf	0.8	10.1	nmf	nmf	nmf	5.5%	43,916
IP	International Paper	-5.5	\$43.53	\$65.30	Materials	8.7	0.7	4.7	19.0	6.8	13.3	281%	4.7%	17,069
KSS	Kohl's Corp	-10.7	\$45.49	\$62.19	Retailing	8.9	0.4	1.3	12.9	5.5	12.8	109%	5.9%	7,122
MOS	Mosaic Co	-11.6	\$19.14	\$38.85	Materials	15.7	0.8	0.9	-0.3	8.7	-4.2	56%	1.0%	7,250
MRK	Merck & Co	-5.5	\$85.98	\$100.22	Pharma, Biotech	17.0	4.8	nmf	31.4	15.1	4.0	nmf	2.8%	218,904
PNC	PNC Financial Services	-5.1	\$150.38	\$177.04	Banks	13.2	nmf	1.8	11.5	nmf	nmf	nmf	3.1%	65,115
RCL	Royal Caribbean Cruises	-5.2	\$126.51	\$162.41	Consumer Services	13.1	2.5	2.5	16.5	11.1	1.3	89%	2.5%	26,520
SLB	Schlumberger Ltd	-11.0	\$35.77	\$64.83	Energy	24.3	1.5	78.7	-33.8	-10.2	7.5	nmf	5.6%	49,524
SYF	Synchrony Financial	-9.4	\$32.63	\$53.21	Diversified Financials	7.6	nmf	1.7	25.8	nmf	nmf	nmf	2.7%	20,097
TGT	Target	-10.8	\$114.32	\$131.10	Retailing	18.3	0.7	5.3	28.7	9.8	5.9	117%	2.3%	57,930
TNP	Tsakos Energy Navigation	-19.0	\$3.53	\$5.83	Energy	nmf	0.5	nmf	-1.3	7.4	nmf	nmf	2.8%	316
TSN	Tyson Foods	-5.6	\$85.93	\$104.85	Food, Beverage & Tobacco	15.7	0.7	nmf	15.0	11.0	4.0	nmf	2.0%	31,397
WBA	Walgreens Boots Alliance	-11.7	\$52.04	\$94.31	Food & Staples Retailing	8.8	0.3	nmf	15.0	12.0	9.7	nmf	3.5%	46,100

As of 1.24.20. nmf=Not meaningful. ROCE = Return on Common Equity. TBV = Tangible book value. EV/EBITDA = Enterprise value to earnings before interest, taxes, depreciation and amortization. FCF Yield = Free Cash Flow Yield

And, given all of the bad news out of late, we close this missive with notes from Saturday's *Intelligent Investor* column in *The Wall Street Journal* by Jason Zweig, in which one of your editor's favorite financial journalists laments the gloomy view of the future that so many 20-somethings have. He specifically mentioned a "smart 22-year-old" who didn't want to invest in an individual retirement account because she couldn't touch it until she turns 59 and a half, saying, "By then the planet will be a rotating cinder!"

Not surprisingly, this attitude weighs on young people's willingness to invest, despite a multi-decade time horizon and often very generous employer incentives to encourage such behavior. It is no doubt an interesting topic...

<https://www.morningstar.com/news/marketwatch/20191224113/this-holiday-gift-could-earn-your-child-52927>

...and Mr. Zweig suggests that the young (and the not so young) check out a new book by Laurence B. Siegel. In *Fewer, Richer, Greener*, Mr. Siegel states, "We are on the verge of the greatest democratization of wealth and well-being that the world has ever known."

As Mr. Zweig writes, "If Mr. Siegel is right, by 2056 (when this young investor will turn 59 1/2), billions of people will be wealthier, healthier and happier than ever before. New technologies in

energy, food, education and medicine will heal the planet and enrich human life. The use of fossil fuels will dwindle; many commodity prices will decline. Frontier markets, including nations in Africa and Latin America, will boom.”

We especially like the concluding paragraphs of Mr. Zweig’s piece:

*Q: At the end of your book, you write: “Apocalyptic thinking is a neural mistake based on our need to survive in a cruelly hostile environment that doesn’t exist anymore.” What do you mean?*

*A: We evolved under conditions in which not only the individual but the whole species were often in danger of extinction. Our neural network says to us all the time: That could be a tiger, or it could be a rabbit, so let’s assume it’s a tiger. In the modern world, though, that often leads us to worry more about some dangers than we need to, because they rarely or never occur anymore.*

*As Mr. Siegel writes, apocalyptic thinking “has always been wrong as a forecast, and it will continue to be wrong.” Here’s hoping young people will take his message to heart, realize that capitalism can be a force for good and stop fearing the future.*

## **Stock Updates**

Jason Clark and Chris Quigley take a look at 11 of our companies that were out with news last week of sufficient importance to trigger a review of their review of their respective Target Prices. Note that all stocks are rated as a “Buy” until such time as they are a “Sell,” while a listing of all current recommendations is available for download via the following link:

<https://theprudentspeculator.com/dashboard/>.

Global health and pharmaceutical concern **Johnson & Johnson** (JNJ – \$148.32) released Q4 results that edged analyst EPS estimates (\$1.88 vs \$1.87). Shares dropped nearly 2% at the open, but recovered modestly throughout the week. The company produced \$82 billion of revenue for the full year (growth of 0.6%) and grew full-year adjusted earnings per share by 6.1% to \$8.68. Management also released guidance for 2020, expecting to grow adjusted earnings by nearly 4% to around \$9.00 per share. Sales are expected to climb higher by nearly 6%, with the strong top-line performance fueling investment in the business throughout the year.

CEO Alex Gorsky commented, “We remain focused on the long term, a mindset we’ve maintained for more than a century; a mindset that is directly linked to our focused execution, our relentless pursuit of innovation, our talented and passionate people, our culture of caring for the world and our unwavering focus on value creation for all our stakeholders. In fact, I’m proud to highlight that 2019 marked our 36th consecutive year of adjusted operational earnings growth for Johnson & Johnson. Now this performance is indicative of the strength of our broad-based business, and we remain focused on driving the next generation of innovation across our entire portfolio in new markets, in markets where we have greater opportunity to compete and in the markets where we lead, which include our 26 platforms that each deliver \$1 billion or more in sales annually.”

26 Platforms / Products over \$1B in Annual Sales

2019 Blockbuster Portfolio



2019 was a year of multiple legal headwinds for JNJ. The company faces liability from the ongoing investigation into the country’s opioid epidemic, along with litigation threats related to its talc and other products. J&J did receive a bit of good news last week, however, in a case regarding antipsychotic drug Risperdal when a Philadelphia judge drastically reduced a massive punitive damage award of \$8 billion that the company was initially ordered to pay in October down to just \$6.8 million. In a statement to *The New York Times*, JNJ said, “The jury did not hear evidence as to how the label for Risperdal clearly and appropriately outlined the risks associated with the medicine, or the benefits Risperdal provides to patients with serious mental illness.”

We still like JNJ overall and still view the company as uniquely situated with unmatched depth and breadth in growing global health care markets. Moreover, there is solid potential for several of its compounds in clinical trials. While headline risk from various legal hurdles continue to weigh on our patience, we are still holding tight to our shares, but are always weighing the risk/reward profile of the stocks we own versus other names that we might want to buy. The high-quality name still carries a dividend yield of 2.6% and trades at nearly 16 times management’s 2020 earnings estimate. Our Target Price for JNJ now stands at \$157.

Health care equipment manufacturer **Abbott Laboratories** (ABT – \$90.40) reported earnings per share of \$0.95, versus the \$0.95 estimate, in fiscal Q4 2019. ABT had sales of \$8.3 billion

(vs. \$8.3 billion est.). Shares moved up following the announcement, reaching an all-time high (they pulled back later in the week), on organic overall sales growth of 7.5% year-over-year and double-digit sales growth in Medical Devices, Established Pharmaceuticals and Core Laboratory Diagnostics. Abbott's FreeStyle Libre, a continuous glucose monitoring system, has doubled its user base each year since it was introduced in late 2017, with a current level of approximately 2 million users. Worldwide sales are near \$2 billion, an increase of 70% from the prior year.

"This was another highly successful year with strong performance across our businesses," said ABT CEO Miles D. White. "We continue to strengthen our leadership positions in some of the largest and fastest-growing areas in health care, and we're entering 2020 with great momentum across our businesses and targeting another year of strong organic sales growth and double-digit EPS growth."

Abbott projects 2022 sales growth of 7% to 8%, and adjusted EPS for the full year 2020 to come in between \$3.55 and \$3.65. For Q1, management expects EPS to be between \$0.40 to \$0.42.

We believe that Abbott should be able to continue to enhance its free cash flow generation, which can be used to improve the balance sheet, return capital to shareholders and invest in the business. All the positives mentioned, we continue to keep a close eye on ABT shares as the valuation isn't exactly cheap at face value (though ABT shares are less expensive than many of its peers), given a forward P/E of about 25. For the time being, our Target Price has been bumped up to \$96.

Despite a pullback on Friday, shares of consumer finance firm **Capital One Financial** (COF – \$104.27) ended last week up nicely following a solid earnings release. For Q4, COF said it had adjusted earnings of \$2.49 per share, versus consensus estimates of \$2.37. Revenue was \$7.43 billion, versus the \$7.35 billion estimate. COF had a net interest margin of 6.95%, net credit card charge-offs of 4.31% (vs. 4.61% a year ago) and credit card delinquencies of 3.93% (vs. 4.04% a year ago). We continue to believe Capital One is one of the best managed banks nationally, and this quarter's strong results reflect its ongoing investments in technology and marketing.

**Company Highlights**



- Net income for the fourth quarter of 2019 of \$1.2 billion, or \$2.25 per diluted common share; full year 2019 net income of \$5.5 billion, or \$11.05 per diluted common share
  - Excluding adjusting items, net income per diluted common share for the fourth quarter of 2019 of \$2.49; full year 2019 of \$12.09<sup>(1)</sup>
- Pre-provision earnings increased 6% to \$3.3 billion for the fourth quarter of 2019 and remained flat year-over-year<sup>(2)</sup>
- Efficiency ratio of 56.03% for the fourth quarter of 2019 and 54.15% for the full year 2019
  - Efficiency ratio excluding adjusting items was 55.16% for the fourth quarter of 2019 and 52.67% for the full year 2019<sup>(3)</sup>
- Operating efficiency ratio of 46.47% for the fourth quarter of 2019 and 46.20% for the full year 2019
  - Operating efficiency ratio excluding adjusting items was 45.60% for the fourth quarter of 2019 and 44.76% for the full year 2019<sup>(3)</sup>
- Adjusting items in the quarter, which are excluded from diluted earnings per share (EPS) and efficiency ratio metrics (see slide 14 for additional information):

	Pre-Tax Impact	Diluted EPS Impact
<i>(Dollars in millions, except per share data)</i>		
Initial allowance build on acquired Walmart portfolio	\$ 84	\$ 0.13
Walmart launch and related integration expenses	48	0.08
Cybersecurity incident expenses, net of insurance	16	0.03

- Common equity Tier 1 capital ratio under Basel III Standardized Approach of 12.2% at December 31, 2019
- Repurchased 10 million common shares
- Period-end loans held for investment increased \$16.5 billion to \$265.8 billion
- Average loans held for investment increased \$12.7 billion to \$258.9 billion
- Period-end total deposits increased \$5.5 billion to \$262.7 billion
- Average total deposits increased \$5.0 billion to \$260.0 billion

Note: All comparisons are for the fourth quarter of 2019 compared with the third quarter of 2019 unless otherwise noted. Regulatory capital metrics and capital ratios as of December 31, 2019 are preliminary and therefore subject to change.  
<sup>(1)</sup> Amounts excluding adjusting items are non-GAAP measures. See Appendix slides 14-15 for the reconciliation of non-GAAP measures to our reported results.  
<sup>(2)</sup> Pre-provision earnings is calculated based on the sum of net interest income and non-interest income, less non-interest expense for the period.

CEO Richard D. Fairbank commented, “In the fourth quarter and for the full year 2019, Capital One continued to post solid results as we invest to grow and to drive our digital transformation. As the many benefit from our technology transformation continue and increase, we are well positioned to succeed in a rapidly changing marketplace.”

While COF shares have had a nice run over the last year (up 32% including dividends), we continue to remain long-term focused and think there is still plenty of upside in the inexpensively valued financial name. The shares currently changes hands below 9 times NTM estimated EPS and for just 90% of book value. We like that COF is a willing and opportunistic asset acquirer in efforts to bolster returns and diversify. Additionally, we like the firm’s focus on managing risks, while improving efficiency, even as it invests to grow and transform itself as banking goes digital. Our Target Price has been boosted to \$134.

Global provider of computer solutions and advanced technologies leader **Int’l Business Machines** (IBM – \$140.56) earned \$4.71 per share in fiscal Q4 2019 (vs. \$4.69 est.). IBM had total revenue of \$21.8 billion, versus the \$21.6 billion estimate. Shares rose 3.4% following the announcement, but retreated in the last two days of the week to bring the week’s gain to 1.6%.

While CEO Ginni Rometty was busy making the media rounds at the World Economic Forum in Davos, Switzerland, CFO Jim Kavanaugh discussed the quarter with analysts at the company’s

Q4 conference call, “In the fourth quarter, we grew revenue at actual rates, and it was up 3% at constant currency, excluding divestitures. Our operating gross margin was up over 2 points, which is the best margin expansion in some time. We delivered \$4.2 billion of operating net income and \$6 billion of free cash flow, and we had \$4.71 of operating earnings per share. We also reduced our debt balance by another \$3 billion in the quarter for a total reduction of \$10 billion since the end of June. This caps off the year with \$77 billion of revenue, \$12.81 of operating earnings per share and about \$12 billion of free cash flow, in line with our expectations.”

Mr. Kavanaugh continued, “We’ve been focused on the next chapter of our clients’ digital reinventions. We acquired Red Hat, modernized our software portfolio and brought these together to create the leading hybrid cloud platform. We are introducing joint GBS and GTS offerings to help clients on their cloud journeys. We brought new innovations to market... With our high-value mix and focus on productivity, we expanded our gross margin, and we had strong free cash flow generation. With this trajectory, in 2020, we expect to grow revenue, operating earnings per share and free cash flow and expand operating gross margin. Within that, we’ll maintain a high level of investment focused on hybrid cloud and data and AI capabilities. We’ll drive productivity and take structural actions, especially in our GTS business. And remember, we’ll continue to face year-to-year headwinds from the divested businesses, especially in the first half. And our P&L will also still have an impact from the Red Hat noncash purchase accounting adjustments, though less than 2019.”

IBM grew quarterly year-over-year revenue by a smidge, which we are thrilled about, as quarterly revenue growth has evaded the company consistently over the past few years. We believe that the Red Hat acquisition is likely to help IBM find its footing and regain some of the value it has lost as competitors, including names we presently have in our portfolios like **Oracle** (ORCL – \$54.07), have swooped in on the company’s cloud business. The company still offers a big 4.6% yield and has been a big buyer of its own shares since 1995 (though repurchase plans are on hold as it pays down debt from the Red Hat acquisition), but we believe there can be some multiple expansion if Big Blue can string together a few quarters of solid growth. While the second decade of the 2000’s was atrocious for IBM relative to the broad indexes, we believe that a clean slate, solid free cash flow and a sub-11 times forward P/E ratio are good starting points for the new decade. Our Target Price for IBM has been hiked to \$185.

Cable and satellite firm **Comcast** (CMCSA – \$44.59) reported earnings per share of \$0.79, versus the \$0.77 estimate, in fiscal Q4 2019. CMCSA had sales of \$28.4 billion (vs. \$28.1 billion est.). Despite the double-beat, shares tumbled following the announcement, as strong Xfinity Mobile growth was outweighed by drops in revenue and EBITDA (earnings before interest, taxes, depreciation and amortization) in the NBCUniversal segment.

CEO Brian Roberts said, “2019 was a busy, productive and exciting year for our company, capped off by a strong fourth quarter, and we’ve already jumped right into 2020 with the debut of our exciting new streaming service, Peacock. It’s a truly differentiated approach to streaming that leverages capabilities from all across our company. As we look to the future, I am confident that the company we have built has all the necessary components to succeed, and our guiding principles remain the same: be leaders in our markets; continuously improve our products and

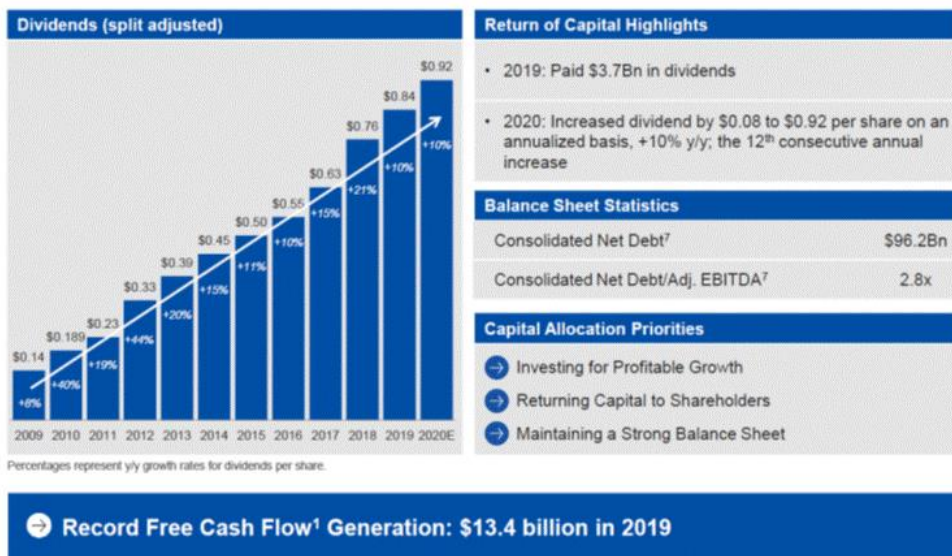
experiences; and build deep, highly valuable recurring customer relationships. Our world-class teams are executing and operating at a high level, all of which allows us to invest in our businesses and deliver consistent results.”

CFO Michael Cavanagh added, “We’re pleased with the progress Sky is making by delivering growth in customer relationships and creating award-winning popular content. We expect these tailwinds to continue in 2020, and but keep in mind, we also expect our results will continue to be impacted by the challenging macroeconomic environment and changes in gambling legislation. All in, before the few hundred million dollars of investment we’ve previously outlined for Sky Q and broadband in Italy, and using today’s foreign exchange rates, we expect Sky’s 2020 EBITDA to be consistent with our reported 2019 results... We generated a record \$13.4 billion in free cash flow and paid \$3.7 billion in dividends to our shareholders in 2019. We also made great progress in leveraging, ending the year at 2.8x net leverage, down from 3.3x at the end of 2018. Deleveraging will remain a top focus for us in 2020, which we will balance with the key investment priorities we have outlined across Cable, NBCUniversal and Sky.”

**AFAM**  
a KOVITZ division

**THE PRUDENT SPECULATOR**  
**CMCSA – Free Cash Flow Machine**

**Free Cash Flow and Capital Allocation**



We continue to like the company’s overall trajectory and think the earnings-related sell-off was overdone. We are interested to start seeing numbers from Peacock, which in our understanding, will have more emphasis on ads via a free version and \$5 per month version, the latter of which has an expanded library and keeps the ads. For \$10 per month, one gets the larger library and no

ads. We like CMCSA's diverse media portfolio (including NBC, Telemundo, E!, NBC Sports Network, Sky), geographically diverse theme parks (Universal Parks & Resorts, including Universal Studios Hollywood) and investments in alternative methods of content delivery (Peacock). We also like the significant free-cash flow generation, forward P/E ratio around 14 and just-increased dividend yield of 2.1%. Our Target Price now stands at \$60.

Semiconductor giant **Intel** (INTC – \$68.47) earned \$1.52 per share in fiscal Q4 2019 (vs. \$1.25 est.). INTC had sales of \$20.2 billion (vs. \$19.2 billion est.). Shares climbed 8.1% following the announcement on an otherwise dismal trading day, pushing the YTD gain to 14.4% and the market capitalization near \$300 billion.

CEO Bob Swan commented, “We exceeded our expectations for Q4 '19, capping off a fourth consecutive record year. In Q4, we generated \$20.2 billion in revenue and \$1.52 in earnings per share, exceeding our guidance by \$1 billion and \$0.28, respectively. For the full year, we delivered \$72 billion in revenue and \$4.87 in EPS. The PC, Data Center, IoT, Memory and Mobileye businesses each set all-time annual revenue records. Several years ago, we began a transformation to reposition the company to take advantage of the data revolution that is reshaping computing. Exiting this quarter, we now have greater than 50% of our revenue coming from our data-centric collection of businesses, but our journey is just beginning. To reach our multiyear goals, we will continuously focus on 3 key priorities: accelerating growth, improving execution and deploying our capital for attractive returns.”

Mr. Swan also gave a chip update, “Our process technology execution continues to improve. In Q4, we ramped our 10-nanometer production and continue to see yields improve. We are planning 9 new product releases on 10-nanometer this year, including our next-gen mobile CPU, a 5G base station SoC, an AI inference accelerator, our first discrete GPU and Xeon for server, storage and networking. We're also on track to deliver 10-nanometer plus this year, our first performance upgrade on 10-nanometer. Our 7-nanometer process remains on track to deliver our lead 7-nanometer product, Ponte Vecchio, at the end of 2021, with CPU products following shortly after in 2022.”

In three to four years, Intel is targeting \$6 in EPS and \$85 billion in revenue with progress towards the goal each quarter in between. Mr. Swan said the company's priorities are to “to accelerate growth, improve execution and thoughtfully deploy our capital.” INTC also expects to buy back \$20 billion of stock over the next four to five quarters.

Intel had significant trouble getting its 10-nanometer chips to production, but the company seems to be getting the program back on track. We continue to like Intel's strong balance sheet, return of capital and deep bench of talent. We continue to favor the company's diversified revenue stream, low levels of debt, forward P/E ratio below 14 and 1.9% dividend yield (the quarterly payment was just increased from 31.5 cents per share to 33 cents). Our Target Price has been elevated to \$74.

With Intel's capital spending plans also exceeding expectations, we have continued to raise our Target Prices for our chip-equipment makers, with recent hikes for **Lam Research** (LRCX –



\$306.54) to \$316, **Cohu Inc.** (COHU – \$24.90) to \$27 and **Kulicke & Soffa** (KLIC – \$28.02) to \$31.

**KeyCorp** (KEY – \$19.27) reported Q4 financial results last week that were largely in line with analyst expectations. Adjusted EPS for the bank holding company came in at \$0.48 on revenue of \$1.6 billion, both numbers right about as expected. Overall, we thought the quarter was solid, highlighted by strong consumer loan growth and flexibility on expenses, which helped offset lighted-than-expected investment banking revenue. CEO Beth Mooney agreed, “Key’s fourth quarter results marked a good finish to another strong year for our company. We achieved our seventh consecutive year of positive operating leverage, supported by solid balance sheet growth, continued momentum in our fee-based businesses and strong expense control. Across our company, we continued to add and expand client relationships, which drove growth in loans, deposits and fees...Our ongoing focus on expense management and continuous improvement resulted in lower expenses for the year and a 140-basis point improvement in our cash efficiency ratio, excluding notable items.”

Looking ahead, Ms. Mooney said, “While we have continued to reduce costs, we remain committed to making strategic investments that will drive future growth and returns. Our recent investments in talent, products and capabilities, including our Laurel Road acquisition in April of last year, have exceeded our expectations, benefiting our top line growth, improving the client experience and driving efficiency...Strong risk management and being disciplined with our capital have also remained top priorities. Credit quality trends remained solid this quarter, and we continue to be diligent in our credit underwriting. We have also returned capital to our shareholders throughout the year in the form of share repurchases and a 9% increase in our common stock dividend.”


As a reminder, Ms. Mooney will be retiring this upcoming May. Current COO Chris Gorman, a 21-year veteran of KeyCorp, will fill the role. The company said that the CEO transition is progressing smoothly and is on track.

**FY2020 Outlook & Long-term Targets**

FY 2020 (vs. FY 2019)	
Average Balance Sheet	<ul style="list-style-type: none"> <li>Loans: up mid-single digit</li> <li>Deposits: up low-single digit</li> </ul>
Net Interest Income (TE)	<ul style="list-style-type: none"> <li>Net interest income: up low-single digit</li> <li>Net interest margin: relatively stable with 4Q19</li> </ul>
Noninterest Income	<ul style="list-style-type: none"> <li>Noninterest income: up mid-single digit</li> </ul>
Noninterest Expense	<ul style="list-style-type: none"> <li>Noninterest expense: relatively stable</li> <li>– Relatively stable outlook for 2020 is relative to 2019 noninterest expense (excluding notable items) of \$3.8 B</li> </ul>
Credit Quality	<ul style="list-style-type: none"> <li>Net charge-offs to average loans: below through-the-cycle range of 40 - 60 bps</li> <li>Provision: expected to exceed net charge-offs reflecting continued loan growth</li> <li>CECL: relatively stable economic outlook</li> </ul>
Taxes	<ul style="list-style-type: none"> <li>GAAP tax rate: in the range of 17% - 18%</li> </ul>

Outlook excludes notable items      Guidance ranges: relatively stable: +/- 2%; low single-digit: 1% - 3%; mid-single digit: 4% - 6%

Long-term Targets			
Positive operating leverage	Cash efficiency ratio: 54% - 56%	Moderate risk profile: Net charge-offs to avg. loans targeted range of 40-60 bps	ROTCE: 16% - 19%



While the stock has traded virtually flat over the past two and a half years, management has committed to steadily raising its dividend payout to 50% of earnings, which have been rising over the period. The dividend yield is now up to 3.8%. Shares continue to be attractively priced, as they trade a bit above 10 times NTM expected earnings. We continue to believe that KEY offers investors stronger growth potential, expense management and capital return than many of its peers. Our Target Price for KEY is \$25.

**Comerica** (CMA – \$64.73) released Q4 earnings of \$1.85 per share Tuesday that beat analyst estimates of \$1.74, bringing full year earnings to \$7.81 per share. CMA experienced 9% EPS growth in 2019, bolstered by a sale of its Health Savings Account business, higher fee income and a robust share repurchase program. With 80% of loans of the floating rate type, lower rates drove a decline in interest income even as management continues to apply hedges to dampen further interest rate risk. While shares ended 2019 at the same level they began, during the year, the bank grew book value by 10%, raised the dividend by 46% and reduced the share count by 11%. Another highlight was an extension by the U.S. Treasury for Comerica to be the exclusive financial intermediary for the Direct Express government benefits card program for an additional 5 years.

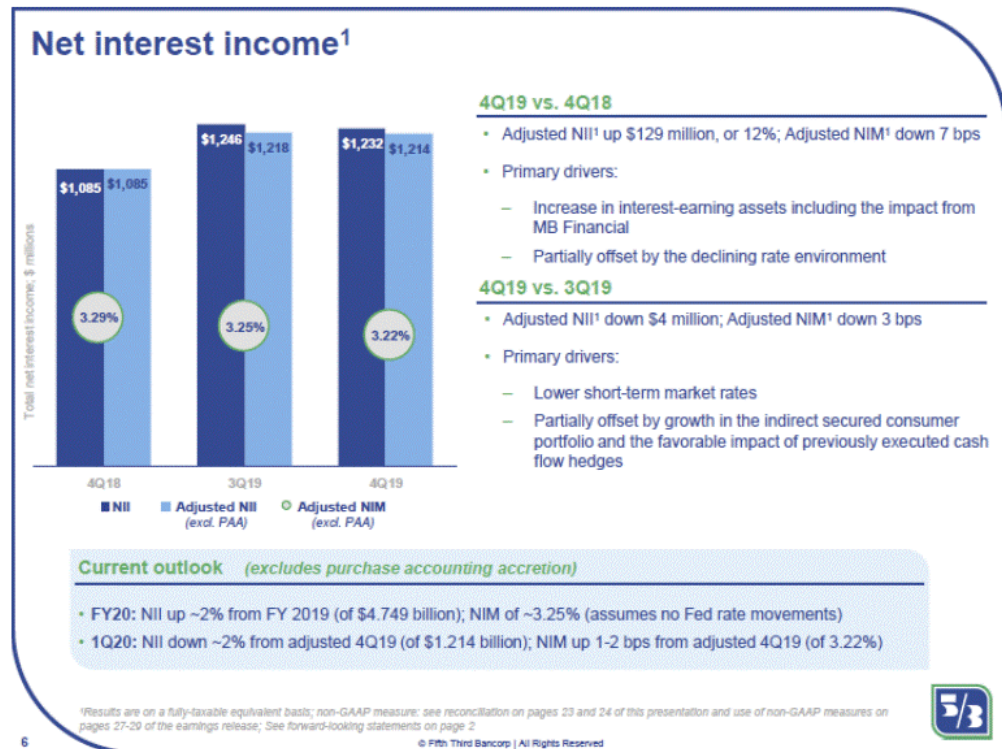
On the earnings call CFO James Herzog gave expectations for 2020, “As far as the first quarter, we expect loan growth for most business lines will be mostly offset by a decline in Mortgage

Banking due to seasonality combined with the slowdown in refi activity. We expect average deposit growth of 1% to 2%. We believe we will have the normal seasonality through the year including the typical first quarter decline. Our goal is to continue to attract and retain long-term customer relationships by offering superior products and services along with the appropriate pricing. As far as noninterest income, we expect growth of about 1%, led by card and fiduciary fees. Our expectation includes declines in certain key categories that had strong growth in 2019 such as customer derivative and warrant income.”

While we know that CMA continues to face challenges related to the interest rate environment, we appreciate the bank’s generous capital returns that are supported by an attractive efficiency ratio and returns on equity in excess of 15%. Despite having one of the most attractive deposit franchises, CMA trades for less than 10 times NTM adjusted EPS estimates and yields 4.1%. We have pared our Target Price to \$99.

**Fifth Third Bancorp** (FITB – \$28.84) reported Q4 adjusted earnings per share of \$0.68 that missed analyst estimates (\$0.72). That said, the bank’s full year earnings came in nearly 33% higher than the previous year, largely a result of its acquisition of MB Financial. Management appears to be on track to realize expected synergies from the deal by the end of Q1 this year. Core return on tangible common equity increased 30 basis points from the prior year to 14.8%, while tangible book value per share increased 10% from last year.

CFO Tayfun Tuzun offered guidance for the current year, “For the full year 2020, we continue to expect core NIM to be 3.25%, consistent with our October guidance and down just 2 basis points from our core 2019 NIM, assuming no Fed rate cuts this year. For the full year, we currently expect net interest income, excluding purchase accounting adjustments, to increase approximately 2%. We expect our first quarter net interest income, excluding purchase accounting adjustments, to decline approximately 2% sequentially, impacted by day counts and the relatively stable loan growth outlook. Our first quarter outlook also assumes partial reinvestment of the investment portfolio cash flows, which may change depending on the environment. Our 2019 noninterest income results demonstrate the increasing benefit of having a platform with a wide scope of product and service capabilities. For the full year 2020, we expect core noninterest income growth of approximately 8%, relative to the adjusted 2019 level of \$2.711 billion, including the expected Worldpay TRA benefit in the fourth quarter. We expect first quarter noninterest income to decline approximately 3%, reflecting seasonally lower mortgage and interchange revenue. Our first quarter forecast also does not include any investment gains. In total, as a result of NII growth and strong increase in fees, we expect to achieve a very strong 4% total revenue growth in 2020.”



We continue to believe that FITB is a good regional banking name to own in a diversified equity portfolio, and while the MB Financial acquisition was a bit pricey, the integration should improve the combined company’s operating leverage potential. Shares are trading at 9.7 times forward earnings estimates and carry a dividend yield of 3.3%. Our Target Price for FITB now resides at \$42.

Shares of **Synchrony Financial** (SYF – \$32.63) fell almost 10% after the consumer financial firm reported Q4 results. Despite posting a better-than-expected bottom line, and revenue that was generally in line with estimates, investors dumped shares as net interest income contracted and initial 2020 NIM guidance was a bit less than hoped, while expenses are likely to be higher. Q4 unadjusted EPS came in at \$1.15 per share, but the company said that \$0.05 resulted via the sale of its Walmart credit-card portfolio (with the sale of said portfolio also hitting net interest income by 7%). That said, the adjusted number still topped expectations of \$1.07.

CEO Margaret Keane commented, “2019 marked another year of significant transformation for Synchrony. During the year we renewed over 50 partnerships and won 30 new business deals, expanded our CareCredit, Auto and Home networks, significantly enhanced the digital experience for our cardholders, and substantially grew our direct-to-consumer deposit platform. The consistent investments we have made in people and technology have propelled our company forward and empowered leading offerings for our partners and enhanced capabilities and user

experiences for our cardholders. Organic growth continues to present the largest opportunity as we have demonstrated in our ability to not only grow existing programs, but also launch new programs with fast-growing partners in new markets. Further, we remain focused on executing a capital allocation strategy that helps to drive growth at attractive risk adjusted returns, while maintaining a strong balance sheet and the ability to continue to return capital to shareholders.”

Ms. Keane’s comment concerning maintaining a strong balance sheet is always music to our ears, as total liquidity (liquid assets and undrawn credit facilities) was \$23.4 billion, or 22.3% of total assets, and the estimated fully phased-in Common Equity Tier 1 ratio under Basel III was 14.1%. It is also important to consider that loans 30+ days past due as a percentage of total period-end loan receivables were 4.44%, compared to 4.76% in the same period last year. Net charge-offs as a percentage of total average loan receivables were 5.15%, compared to 5.54% last year, excluding the newer PayPal Credit program and the Walmart portfolio. Additionally, allowance for loan losses as a percentage of total period-end loan receivables was 6.42%, compared to 6.9% in Q4 2018.

While expenses may be up, at least in early 2020, we would argue that it is worth it given that much will be driven by investments needed to launch exciting new programs with Venmo and Verizon. Additionally, we continue to believe SYF is a long-term winner and is well positioned to benefit from relationships with faster growth digital partners like PayPal and Amazon. Shares trade at just 8 times NTM adjusted EPS consensus estimates and yield 2.7%. Our Target Price is now \$53.

**Old National Bank** (ONB—\$18.17) released Q4 earnings of \$0.29 per share Tuesday that missed analyst estimates of \$0.35, bringing full year earnings to \$1.38 per share. The stock sold off at the market open to below \$18, before recovering modestly throughout the week. The Midwestern regional bank rolled out a new strategic plan called the ONB Way designed to increase efficiencies across the organization while investing to enhance technology infrastructure. ONB saw record commercial loan production and lowered deposit costs by 9 basis points to 43 basis points in the quarter.

### Our Vision for the ONB Way

*We are a leading commercially-oriented regional bank with a distinctive client-centric value proposition based on strong relationships, streamlined operating model, and an exceptional work environment that empowers our team members to deliver their best.*

### Six Key Pillars Of Our ONB Way Strategy

**OLD NATIONAL** Old National is a commercially-oriented regional bank that consistently delivers top quartile performance to clients, team members, shareholders and communities

**1** Commercial salesforce aligned to client's size or loan type

- Relationship Manager (RM) aligned to segments based on clients' revenue size
- Dedicated units for specialized lending and select industry verticals to develop deeper expertise
- Increased Treasury Management (TM) cross-selling with enhanced pricing discipline and collaboration model across RMs and TM officers

**2** Community Banking offering tailored to the markets we operate in

- Serving communities of clients and small businesses through products and services that meet their needs
- Full range of distribution channels to meet clients where they are
- Cultural shift in banking centers to engage clients through sales
- Efficient physical presence tailored to strategic market archetypes

**3** Banking led Affluent & HNW offering to serve eligible clients

- Private Bankers as the primary relationship contact
- Single team of Wealth Advisors, leading with financial planning and with deep investment expertise
- Team approach to more complex relationships, with dedicated Financial Planners and specialists
- Close partnership with other business, especially Commercial and Mortgage

**4** Risk management processes that align complexity with amount of risk taken in each of our segments, leading to overall better client experience, improved cycle times and enhanced efficiency

**5** Streamlined operating model, optimized procurement function, and enhanced technology infrastructure to provide scalability across the entire bank via centralized functions and value-based orientation

**6** Sales and performance orientation, centered around client needs, and culture of full empowerment and accountability

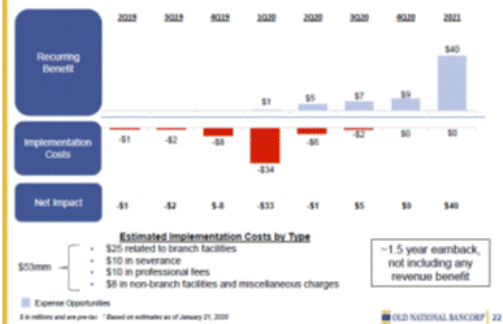
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### The ONB Way – Major Initiatives

	Objectives	Initiatives
Revenue Enhancements (Expected Net Revenue Improvement in 2021)	Accelerate growth in commercial banking	<ul style="list-style-type: none"> <li>Segmentation of portfolio and salesforce</li> <li>Create high-potential industry verticals</li> <li>Targeted cross-selling of Treasury Management</li> </ul>
	Deepen client relationships	<ul style="list-style-type: none"> <li>Improve analytics to better identify opportunities</li> <li>Increase consumer lending opportunities</li> </ul>
	Enhance affluent and high net worth client offerings	<ul style="list-style-type: none"> <li>Team approach led by private banker</li> <li>Emphasis on financial planning</li> </ul>
Expense Opportunities	Streamline credit approval process	<ul style="list-style-type: none"> <li>Establish a Credit Center that will process more efficiently and effectively</li> <li>Automate tasks within the Credit monitoring</li> </ul>
	Rationalize real estate	<ul style="list-style-type: none"> <li>Reduce office and operations space</li> <li>Consolidation of 31 banking centers</li> </ul>
	Streamline reporting layers	<ul style="list-style-type: none"> <li>Flatten organizational structure</li> <li>Consolidation of functions and reduced duplication</li> </ul>
	Improve back room processes	<ul style="list-style-type: none"> <li>Implement new technology and automate labor intensive activities</li> </ul>

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### The ONB Way – Projected Financial Impact<sup>1</sup>



CEO James Ryan gave the following color around the ONB way strategy, “In August of 2019, we set out to build a banking plan was — that was to deliver 3 key objectives. First, transform Old National to a leading, commercially oriented regional bank with a distinctive client-centric value proposition delivered through a client segment-focused organization. Secondly, lay the foundation to be a top-performing independent bank by streamlining our operating model and strengthening our risk and credit processes to provide a seamless client experience. Thirdly, improve our operating leverage, invest in our operational IT infrastructure to meet our clients where they are and ensure that we’re keeping pace with technology and client digital expectation through a balanced portfolio of revenue and cost initiatives to help us deliver top quartile performance.”

The interest rate environment remains a headwind for most banks, and for Old National in particular, given that interest income accounts for 75% of total revenue. Still, we are encouraged by the bank’s focus on areas that it can control like expense management with plenty of runway for improvement. ONB’s growing deposit base also appears an area of strength given the low and shrinking cost of funds. Shares yield 3.1% after the Board’s latest dividend increase of 7.7% last week, and trade in line with book value. Our Target Price has been trimmed to \$22.