Hendershot INVESTMENTS

7-27-20

WEEKLY UPDATE

Economic and Market Performance

MARKET INDEX	CLOSE 7-24-20	WEEK GAIN/LOSS	Y-T-D GAIN/LOSS
DJIA	26,469.89	-0.8%	-7.2%
S&P 500	3,215.63	-0.3%	-0.5%
NASDAQ	10,363.18	-1.3%	+15.5%

Initial jobless claims for the week ending July 18 increased by 109,000 to 1.416 million, which is the 18th straight week they have exceeded one million. The increase in initial claims reflects the impact of states pausing or rolling back their reopening activity due to the rise in coronavirus cases.

Existing home sales surged 20.7% in June to a seasonally adjusted annual rate of 4.72 million. That is the largest monthly increase on record. The inventory of existing homes continues to be constrained which is leading to higher prices amid strong demand due to historically low mortgage rates.

The stock market pulled back last week on worries about renewed tensions between China and the United States and the lack of progress on another fiscal stimulus bill in Washington. Last week, the Dow pulled back 0.8%, the S&P 500 dipped 0.3% and the NASDAQ declined 1.3%.

HI-Quality Company News

GENTEX CORPORATION

Gentex-GNTX reported second quarter net sales declined 51% to $229.9 million with a net loss of $2.4 million compared to net income of $109 million in the prior year quarter. The impact of COVID-19 created extended shutdowns in the global automotive industry resulting in the most severe change in demand in a very short period that Gentex has ever experienced. The company took immediate actions to reduce costs given the dramatic change in demand. Gentex maintains a strong balance sheet with no long-term debt and $585 million in cash and investments as of quarter end. Due to the pandemic, Gentex expects light vehicle production to decline 7% for the second half of 2020 and 20% for the full year 2020. Management expects second half sales to approximate $865 million to $915 million. Despite the decrease in production, management is optimistic that the forecasted improvements in light vehicle production throughout the second half of the year, in addition to their significant cost initiatives achieved during the second quarter, will allow the company to return to more normalized gross and operating margins during the second half of the year.

TSC TRACTOR SUPPLY CO

Tractor Supply-TSCO plowed up exceptional growth in the second quarter with sales jumping 35% to $3.2 billion, net income growing 54% to $339 million and EPS climbing 61% to $2.90. Comparable store sales growth increased an impressive 30.5% with strong double-digit growth across all product categories and geographic regions. Strong sales of big-ticket items like lawn mowers, trailers, kayaks and power washers during the quarter

contributed to the surge in sales. E-commerce sales more than tripled during the quarter. The COVID-19 pandemic and great spring weather had a significant impact on consumer demand as customers focused on the care of their homes, land and animals. The government stimulus checks helped provide customers with buying power as customers shifted their buying patterns from traveling and dining out to backyard living and pet care. Backyard poultry, gardening and bird feeding products sold strongly. Pet adoption reached record levels during the pandemic which led to increased demand for pet food. The company gained new customers at the fastest rate in company history with 4.3 million new customers during the quarter. Free cash flow more than tripled during the first half of the year to $907 million. During the first half, the company paid $81.5 million in dividends and repurchased $263 million of its common stock. The company's strong balance sheet with robust operating cash flows provides the company with significant financial flexibility. The company is in a very strong liquidity position with about $1.3 billion in cash and investments. For the third quarter, management expects comparable store sales growth will moderate to a still high range of 12% to 18% with net sales expected in the range of $2.3 billion to $2.4 billion and EPS expected in the range of $1.15 to $1.35. The company expects the impact of COVID-19 will be a significant factor on results until mid-year 2021, and they are taking actions to capitalize on opportunities in their business and to emerge from the crisis stronger than ever thanks to higher technology and store productivity initiatives. **Tractor Supply's stock has soared this year along with its profits and is one of the best performing stocks in the S&P 500. With the stock now appearing fully valued, we decided to harvest a bumper crop of profits by trimming back our position.**

Microsoft-MSFT reported fourth quarter sales increased 13% to $38 billion with net income and EPS decreasing 15% to $11.2 billion and $1.46, respectively. Excluding a $450 million charge related to the closure of Microsoft retail stores during the quarter and a $2.6 billion tax benefit in 2019, net income and EPS increased 5% and 7%, respectively. COVID-19 positively impacted Microsoft's Productivity and Business Processes and Intelligent Cloud segments, with increased cloud usage and demand as customers continued to work and learn from home. LinkedIn was negatively impacted by the weak job market and reductions in advertising spend. In the More Personal Computing segment, Windows OEM, Surface and Gaming benefited from increased demand to support work-, play-, and learn-from-home scenarios, while Search was negatively impacted by reductions in advertising spend. During the quarter, Microsoft generated $13.9 billion in free cash flow, up 16% from last year, with the company returning nearly $9.7 billion to shareholders through dividend payments of $3.9 billion and share repurchases of $5.8 billion. For the full year, Microsoft reported sales increased 14% to $143 billion with net income increasing 13% to $44.3 billion and EPS up 14% to $5.76. During fiscal 2020, Microsoft generated a stellar 37.4% return on shareholders' equity and $45 billion in free cash flow, up 18% from last year, driven by improving profit margins and operating leverage across the business. Microsoft returned $38 billion to shareholders during the fiscal year through dividends of $15 billion and share repurchases of $23 billion. The company ended the fiscal year with nearly $137 billion in cash on its AAA-rated balance sheet. Looking ahead to the first fiscal quarter of 2021, management expects continued strong usage and consumption in its cloud platform, as well as continued benefit of work, learn and play from home, albeit at a moderated rate as stay-at-home guidelines ease around the globe. Management expects small- and medium-sized business weakness to continue, primarily in Office and Windows OEM.

SEI Investments-SEIC reported second quarter revenues declined 2% to $400.6 million with net income down 20% to $101 million and EPS down 17% to $.68. Revenues declined due to lower assets under management from the carryover effect of the sharp market downturn during March 2020. Average assets under management, excluding LSV, declined $1.8 billion, or 1%, to $226.8 billion during the second quarter. This decline was partially offset by increased fees from higher assets under administration. The average assets under administration increased $49.2 billion, or 8%, to $672.8 billion during the second quarter. Earnings were impacted by increased consulting costs related to continued investments in new business opportunities. Earnings from LSV decreased by $9.5 million, or 25%, to $28.3 million in the second quarter due to lower assets under management in this

business as the deep value investing strategy is not popular right now resulting in negative cash flows from existing clients and client losses. During the quarter, SEI Investments generated $145.3 million in free cash flow and repurchased 1.6 million shares of its common stock for $89.5 million at an average price of about $54.45 per share. The company ended the quarter with a strong balance sheet with more than $865 million in cash and investments and no long-term debt. Over its 50-year history, SEI Investments has always focused on the long term. While the company is facing short-term headwinds from the COVID-19 disruption, management is confident they will weather today's challenging environment and emerge even stronger.

Biogen-BIIB reported second quarter revenues rose 2% to $3.7 billion with net income up 3% to $1.5 billion and EPS jumping 22% to $9.59 on significantly lower shares outstanding. Using its strong cash flows from operations, including $1.9 billion in the second quarter, Biogen repurchased 9 million shares during the second quarter for $2.8 billion at an average price of $313 per share. The company has $1.25 billion remaining authorized for future share repurchases. The company ended the quarter with a solid balance sheet with $5.25 billion in cash and investments and $7.4 billion in long-term debt. During the quarter, Biogen completed its submission to the FDA for aducanumab to treat Alzheimer's disease in the U.S. If it is approved, it would be the first therapy to reduce the clinical decline in Alzheimer's disease. Biogen is continuing to build a multi-franchise portfolio of products based on their expertise in neuroscience with near-term opportunities in other areas such as ALS, Parkinson's, ophthalmology, lupus, stroke and biosimilars. Research and development expense increased 34% during the quarter to $648 million. Biogen updated its 2020 financial guidance with revenue expected to be in the range of $13.8 billion to $14.2 billion, which is slightly lower than previously expected due to the impact of COVID-19. The 2020 EPS outlook was raised to a range of $32.00 to $34.00 based on better than expected first half results in earnings.

Canadian National Railway-CNI reported second quarter revenue declined 19% to C$3.2 billion with net income skidding 60% to C$545 million and EPS dropping 59% to C$.77. These results reflect the adverse impact of the pandemic as well as a one-time charge related to the sale of non-core rail lines. The decrease in revenues was mainly due to lower volumes across most commodity groups caused by the COVID-19 pandemic and lower fuel surcharge rates, which were partly offset by increased shipments of Canadian grain, higher Canadian coal exports as well as freight rate increases. Volume significantly declined beginning in mid-March as the pandemic resulted in economic lockdowns and bottomed in May with sequential improvement seen since then. Management quickly and aggressively rightsized resources by furloughing 26% of employees and reducing active railcars by 14% with 14,500 railcars and 500 locomotives in storage. With volume now slowly improving, CNI is recalling train crews. During the quarter, the company's fuel efficiency improved to record levels with fuel costs down nearly 50%. During the first half of the year, free cash flow nearly doubled to $1.6 billion with the company paying $817 million in dividends. Management is proud that they were able to increase the dividend 7% despite the recession. While the share buyback program is currently on pause, they will reassess it on an ongoing basis. CNI did an opportunistic debt issuance of C$600 million during the quarter at a favorable annual interest rate of 2.45% for 30 years. Canadian National has the best investment credit rating in the industry. With a strong financial position and a commitment to contribute to the economic recovery, the company announced it will purchase about 1,500 new, efficient, high-capacity, covered hopper cars to expand their grain export business for delivery in January of 2021 as record grain shipments are expected. This is part of the company's $2.9 billion capital investment plan for 2020.

Ulta Beauty-ULTA provided a COVID-19 update to its operations. Ulta Beauty has completed its phased reopening process and will require all guests and associates to wear facial coverings when in the stores. To date, approximately 50% of furloughed employees in April have been reactivated. The company is optimizing their real

estate portfolio by temporarily reducing new store openings to 30 in fiscal 2020 and closing 19 stores, with the goal to operate between 1,500 to 1,700 Ulta Beauty stores in the U.S. As new store opening plans are finalized for fiscal 2021, the company anticipates opening additional new stores in the U.S. and in mid-2021 will make its entry to Canada with several stores.

BERKSHIRE HATHAWAY INC.

Berkshire Hathaway-BRKB recently bought roughly $813 million worth of Bank of America stock. Berkshire purchased roughly 33.9 million of the bank's shares at an average price of $23.99 per share, boosting its stake by more than 3% to about 981.7 million shares.

****

As expected, many companies are reporting dismal second quarter results due to the impact of the global pandemic and lockdowns of the global economy. As **Gentex** noted, it was the most severe change in demand in a very short period that most companies have ever experienced. However, as **Canadian National Railway** explained, volume appeared to have bottomed in May with sequential improvement seen since then. Aggressive cost-cutting in response to the dramatic drop in demand will enable these companies to return to more normalized profits as the economy recovers in the second half of the year.

At the same time, several of our ***HI-***quality companies reported exceptional financial results during the pandemic, notably **Tractor Supply** with 35% sales growth and 61% EPS growth as customers used their stimulus checks on their home, land and pets during the lockdown. **Microsoft** also benefited from the rapid shift to remote work, play and learn during the pandemic and booted up $13.9 billion in free cash flow during the past quarter, ending their fiscal June year with a whopping $137 billion in cash and investments after paying $15 billion in dividends and repurchasing $38 billion of their common stock during the fiscal year.

While facing the headwinds of the pandemic, our ***HI***-quality companies have the financial strength to continue to pay dividends, repurchase shares and invest in their business for the future. **Biogen** is increasing their R&D expenditures 34% as they build a multi-franchise portfolio of products based on their expertise in neuroscience with near-term opportunities in areas such as Alzheimer's disease, ALS, Parkinson's, ophthalmology, lupus, stroke and biosimilars.

SEI Investments summed up what many of our companies have been saying with the expectation that they will emerge from the COVID-19 crisis stronger than ever thanks to their long-term focus, durable business models, financial flexibility and experienced management teams.

If you have any questions, please let us know.

Sincerely,

Ingrid R. Hendershot

Ingrid R. Hendershot, CFA
President