10-26-20

WEEKLY UPDATE

Economic and Market Performance

MARKET INDEX	CLOSE 10-23-20	WEEK GAIN/LOSS	Y-T-D GAIN/LOSS
DJIA	28,335.57	-0.9%	-0.7%
S&P 500	3,465.39	-0.5%	+7.3%
NASDAQ	11,548.28	-1.1%	+28.7%

New jobless claims dropped below 800,000 last week to 787,000. This is the first drop below 800,000 since the pandemic began but claims remain historically high. Continuing jobless claims dropped to 8.373 million from 9.397 million during the prior week. The lower continuing claims likely reflect not a rise in re-hiring but rather an increase in the number of individuals exhausting regular state aid and moving to the Pandemic Emergency Unemployment Compensation program, which provides another 13 weeks of benefits.

Total housing starts increased 1.9% month-over-month in September to a seasonally-adjusted annual rate of 1.415 million units. Total building permits jumped 5.2% to 1.553 million. Robust growth in both single-unit starts and permits reflects underlying strength in the market for single-family homes.

Existing home sales increased 9.4% month-over-month in September to a seasonally-adjusted annual rate of 6.54 million, bolstered in part by a 34% annual increase in sales in vacation destination counties. September marked the fourth consecutive month of positive sales gains. Total sales in September were up nearly 21% from a year ago, reflecting strong demand for existing homes.

The Conference Board's Leading Economic Index increased 0.7% in September following an upwardly revised 1.4% increase in August. Strength among the leading indicators has become somewhat more widespread, although the slower pace versus August points to a possible slowdown in recovery momentum entering the fourth quarter.

Rising coronavirus cases and continued haggling over the fiscal stimulus bill weighed on the markets last week. For the week, the Dow declined 0.9%, the S&P 500 dropped 0.5% and NASDAQ fell 1.1%.

HI-Quality Company News

GENTEX CORPORATION

Gentex-GNTX reported third quarter net sales dipped 1% to $474.6 million with net income up 5% to $117.1 million and EPS motoring 9% higher to $.48. Despite the pandemic, sales during the quarter were the second highest sales quarter in company history as the automotive market recovered sharply throughout the quarter. Third quarter volumes increased so quickly that salaried employees volunteered to help build parts to ensure Gentex was able to meet customer orders. Gross margin expanded 200 basis points to 39.7% during the quarter driven by the strength in orders and structural cost reductions that took place in the second quarter. Gentex expects strong margin performance to continue in the fourth quarter and into 2021 and beyond. During the third quarter, the company repurchased 1.2 million shares of its common stock at an average price of $26.93 per share with 11.9 million shares remaining authorized for future share repurchases. The company maintains a strong balance sheet with more than $600 million in cash and investments, no long-term debt and $1.9 billion in shareholders' equity. Based on the strong third quarter results, management raised the second half sales and gross margin outlook for 2020 to a range of revenues of $940 million to

$960 million from the previous guidance of $865 million to $915 million with gross margins now expected to range between 39% to 40% from previous expectations of 36% to 37%. While the COVID-19 pandemic continues to create significant uncertainty, the very rapid recovery in light vehicle production has management cautiously optimistic about the trends in the economy heading into 2021 with revenue sales growth expected in the range of 15%-20% in 2021.

Cisco's-CSCO video-conferencing app Webex recorded 590 million participants in September and is on track to host over 600 million this month, nearly double the numbers recorded in March when countries started shutting down due to the pandemic. After offices started to close due to COVID-19, people switched on video conferencing platforms. Webex has a new product for schools that features the ability to host a large classroom, split the class into small groups, and bring it back together. Cisco also plans to roll out a feature to filter background noise such as a barking dog or the sound of a passing car from an ongoing meeting.

Intel-INTC reported third quarter sales declined 5% to $18.3 billion with net income short-circuiting 29% lower to $4.3 billion and EPS down 24% to $1.02. These results exceeded management's expectations despite pandemic-related impacts in significant portions of the business. Massive demand shifts due to economic uncertainty related to COVID occurred in the Enterprise and Government segment of the Data Center Group. Overall, Datacentric revenue declined 10% while PC-centric revenue rose 1% during the quarter. Operating income declined 22% during the quarter due to lower average selling prices resulting from business mix shifts and higher platform costs. Through the first nine months, free cash flow increased 29% to $15.1 billion. With the company's strong balance sheet and cash flows, Intel paid dividends of $4.2 billion and repurchased $14.2 billion of its common stock. For the full 2020 year, management raised their revenue and earnings guidance with record revenues of approximately $75.3 billion and EPS of $4.55 expected. Free cash flow is expected in the range of $18.0 to $18. 5 billion, representing a high free cash flow yield of about 9%. As previously announced, Intel plans to sell its NAND business for $9 billion which will deliver 100-200 basis points of future gross margin accretion. The proceeds will be reinvested in artificial intelligence (AI), 5G networks and edge computing which should spur future growth.

Tractor Supply-TSCO rang up a 31.4% jump in sales to $2.61 billion with net income plowing ahead 56% to $190.6 million and EPS increasing 59% to $1.62. The COVID-19 pandemic continued to provide significant tailwinds on consumer demand in the third quarter across all major product categories as customers focused on the care of their homes, land and animals. Comparable store sales increased 26.8%, versus a 2.9% increase last year, driven by comparable average transaction count and ticket growth of 14.3% and 12.5%, respectively. Robust comparable store sales growth reflects strong demand for everyday merchandise, including consumable, usable and edible products, and strong growth for summer seasonal categories. All geographic regions of the Company had strong comparable store sales growth. In addition, Tractor Supply's e-commerce sales experienced triple-digit percentage growth. Tractor Supply opened 23 new Tractor Supply stores and three new Petsense stores in the third quarter of 2020. Year-to-date, Tractor Supply generated $844 million in free cash flow, up from $270 million last year, boosted by the increase in net income and efficient working capital management. Year-to-date, Tractor Supply returned $391 million to shareholders through dividend payments of $128 million and share repurchases of $263 million at an average cost per share of $90.77, prior to the suspension of the share buyback program. Tractor Supply ended the quarter with $1.1 billion in cash, $2.8 billion in long-term debt and operating lease liabilities and $1.9 billion in shareholders' equity. In the fourth quarter, management expects net sales in the $2.6 billion to $2.7 billion range (up 34% at the midpoint) on a 15% to 20% comparable store sales increase. Net income is expected in the $163 million to $175 million range (up 38% at the midpoint) and EPS is expected in the $1.37 to $1.47 range (up 39% at the midpoint). Post-COVID, management's long-term goal is to grow sales 6% to 7% annually on 4% to 5% comparable sales growth with EPS growing 8% to 10% annually. Over the next five years, Tractor Supply expects to generate $3.5 billion in free cash flow and return $4 billion to shareholders through opportunistic share repurchases and a targeted dividend payout ratio of 30%.

Genuine Parts-GPC reported third quarter revenues declined 3% to $4.4 billion. Excluding divestitures, revenues rose 0.8%. Net earnings from continuing operations motored 10% higher to $232.9 million with EPS up 11% to $1.61. This solid performance was driven by strengthening sales trends in both the Automotive and Industrial segments. Continued gross margin expansion and significant cost savings led to operating margin expansion in each of the businesses. Strong free cash flow more than doubled during the first nine months to $1.3 billion thanks to the higher earnings, effective working capital management and the sale of receivables. Management remains disciplined in their capital allocation. Through the first nine months, the company has paid $339 million in dividends with a current dividend yield of 3.3%. The dividend was increased 4% in 2020 and has been increased for 64 consecutive years. To preserve cash during the pandemic, the company reduced its capital expenditures 35%-50% to an estimated range of $150 million to $200 million for the year and temporarily suspended share repurchases through the end of the year. Genuine Parts continues to target small, bolt-on acquisitions for the balance of the year. Given the continued lack of visibility caused by the pandemic, the company is not providing annual guidance updates until the macro-economic environment stabilizes further. However, management is positioning the company for sustained long-term growth and improved profitability.

SEI New ways. New answers.®

SEI Investments-SEIC reported third quarter revenues rose 2% to $424.9 million with net income down 16% to $111.1 million and EPS declining 13% to $.75. Revenues from asset management, administration and distribution fees increased primarily from higher assets under management due to positive cash flows from new and existing clients in the Investment Managers segment. The average assets under administration increased 13% to $738.8 billion during the quarter. The average assets under management, excluding LSV, increased 6% to $246.1 billion. The increase in operational expenses was primarily due to increased consulting costs related to continued investments in new business opportunities such as the One SEI strategy and IT Services offering as well as increased personnel costs to service new clients in the Investment Managers segment. Earnings from LSV decreased 25% to $28.3 million due to lower assets under management from negative cash flows from existing clients, market depreciation and client losses. During the third quarter, the company capitalized $5.4 million of software development costs with amortization expense of $10.9 million. The tax rate increased to 21.4% in the third quarter compared to 18.9% in the prior year period. Free cash flow was $333 million during the first nine months of 2020. During the third quarter, the company repurchased 2.1 million shares of its common stock for $108.7 million at an average price of $51.54 per share. The company maintains a strong balance sheet with more than $884 million in cash and investments and no long-term debt.

Biogen-BIIB reported third quarter revenues declined 6% to $3.4 billion with net income dropping 55% to $701.5 million and EPS down 47% to $4.46. These results were impacted by the launch of multiple generics of Biogen's MS drug, TECFIDERA, with generic prices discounted 90%. In addition, third quarter results included a $601 million R&D charge related to Biogen's collaboration with Denali Therapeutics as the companies work together on a treatment for Parkinson's disease. On Nov. 6, Biogen is looking forward to participating in the aducanumab Advisory Committee meeting with the FDA on the priority review of Biogen's application for its treatment of Alzheimer's disease. Biogen has also submitted a Marketing Authorization for aducanumab in Europe and is in formal discussions in Japan for the treatment. If approved, aducanumab would become the first therapy to meaningfully change the course of Alzheimer's disease. Free cash flow declined 10% during the first nine months to $4.3 billion. In the third quarter, Biogen repurchased approximately 4.5 million shares of the company's common stock for a total value of $1.25 billion at an average cost of about $277.77 per share. Biogen's Board of Directors recently authorized a new $5 billion repurchase program. Biogen lowered its sales and earnings outlook for 2020 due to significant erosion of TECFIDERA's financial results reflecting stiff generic competition. For the 2020 full year, revenue is now expected to be in the range of $13.2 billion to $13.4 billion with EPS expected in the range of $25.50 to $26.50.

Canadian National Railway-CNI reported third quarter revenue declined 11% to $3.4 billion with net income dropping 18% to $985 million and EPS rolling 17% lower to $1.38. The operating ratio was 59.9% during the quarter, an increase of 2%. The lower results were primarily due to lower volumes across most commodity groups caused by the ongoing effects of the COVID-19 pandemic. The one bright spot was record shipments of Canadian grain with seven months of record exports. With the potential for a bumper crop of Canadian grains this year, CNI expects this will fuel growth in the fourth quarter and into 2021. The railroad remains nimble and responsive to market demand and is capitalizing on sequential volume improvements in key markets, including lumber and automotive, throughout the third quarter. CNI is bringing back crews and trains in a methodical way while focusing on operational efficiencies with an all-time quarterly record set for fuel efficiency during the quarter. Free cash flow increased 38% during the first nine months of the year to $2.1 billion with the company expecting free cash flow to top $2.5 billion for the full year. During the first nine months, the railroad has paid $1.2 billion in dividends and boasts uninterrupted dividend growth since 1995. Management is maintaining financial discipline as they continue to pause share repurchases which they will reassess on an ongoing basis. With good momentum going into the fourth quarter, management is optimistic about 2021.

Alphabet

The Department of Justice — along with eleven state Attorneys General — filed a civil antitrust lawsuit to stop Google, a unit of **Alphabet-GOOGL**, from unlawfully maintaining monopolies through anticompetitive and exclusionary practices in the search and search advertising markets and to remedy the competitive harms. Google responded that the lawsuit by the Department of Justice is deeply flawed. People use Google because they choose to, not because they're forced to, or because they can't find alternatives. Google believes this lawsuit would do nothing to help consumers. To the contrary, it would artificially prop up lower-quality search alternatives, raise phone prices, and make it harder for people to get the search services they want to use.

****

Financial results from our ***HI***-quality companies this past week reflected Tractor Supply's strong double-digit growth in sales and earnings, long track records of dividend growth from Genuine Parts and Canadian National Railway, substantial share repurchase programs from SEI Investments and Biogen, a high 9% free cash flow yield from Intel and an improving economic outlook from Gentex with 15%-20% sales growth expected in 2021.

If you have any questions, please let us know.

Sincerely,

Ingrid R. Hendershot

Ingrid R. Hendershot, CFA
President