CFRA

THE OUTLOOK

INTELLIGENCE FOR THE INDIVIDUAL INVESTOR

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The Outlook will not be published on Monday, July 3. The newsletter will return on Monday, July 10, 2023. We wish everyone a happy and safe Independence Day!

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Second-Half Outlook

Encouraging mid-year momentum

Sam Stovall, *CFRA Chief Investment Strategist*

Despite ongoing uncertainty surrounding a possible recession, exacerbated by a still hawkish-sounding Fed, an earnings recession, narrow S&P 500 leadership, and an array of steeply inverted yield curves, the equity markets continue to climb a wall of worry. Indeed, the S&P 500 closed more than 20% above its prior bear market low on June 8, 2023, joining the DJIA, Nasdaq-100, and Nasdaq Composite in confirmed bull markets. What's more, with a surprisingly strong H1 2023 nearly in the books, history suggests, but does not guarantee, that H2 market and sector gains could be equally optimistic. Indeed, since 1945, while the S&P 500 gained an average of 4.2% during all H2s, rising in price during 69% of all years, whenever the market's H1 return exceeded 10%, the S&P 500 posted an average H2 advance of 8.0%, and gained in price 82% of the time.

Even with the typically challenging third quarter since 1945, in which the S&P 500 rose in price just 61% of the time versus an average of 67% for all quarters, the market was up 74% of the time in Q3 following positive H1s. Better still, the subsequent Q4 recorded price gains 87% of the time versus 79% for all years. Finally, since 1990, all sizes, styles, sectors, and 92% of all sub-industries gained in price in H2 following an S&P 500 rise in H1. Even though there remains the possibility of elevated volatility in Q3, should the Fed hike rates in July and continue to pressure GDP growth and employment trends, CFRA sees investors looking beyond the near-term weakness and focusing on projected improvements in GDP growth and earnings increases in 2024. As a result we see share prices closing 2023 at 4,575 and reaching 4,820 by this time next year.

Representative companies from this list of S&P 500 sub-industries with the highest H2 returns are: Applied Materials Inc. (AMAT 139 ****), Broadcom Inc. (AVGO 842 ****), The Home Depot Inc. (HD 301 ***), Corteva Inc. (CTVA 58 ****), Palo Alto Networks Inc. (PANW 249 *****), T-Mobile US Inc. (TMUS 134 *****), Biogen Inc. (BIIB 294 ****), and The Charles Schwab Corporation (SCHW 53 *****). ■

S&P 500 SECTOR/SUB-INDUSTRY PRICE RETURNS FOLLOWING POSITIVE FIRST HALVES

REGIONS/SIZES/SECTORS	% CHANGE	BEST S&P 500 SUB-INDUSTRIES	% CHANGE
Information Technology	11.5	Semiconductor Materials & Equip.	15.6
Nasdaq Composite	**10.3**	Semiconductors	15.5
S&P 500 Growth	**8.5**	Home Improvement Retail	14.5
Health Care	7.5	Fertilizers & Agricultural Chemicals	13.3
S&P MidCap 400	**7.3**	Systems Software	12.2
S&P 500	**6.8**	Wireless Telecom. Services	11.6
Consumer Discretionary	6.5	Biotechnology	11.1
S&P 500 Value	**6.3**	Investment Banking & Brokerage	10.5
Financials	6.2	**WORST S&P 500 SUB-INDUSTRIES**	**% CHANGE**
S&P SmallCap 600	**6.2**	Apparel, Access. & Luxury Goods	0.1
Consumer Staples	6.2	Gold	(0.2)
Industrials	5.8	Other Specialty Retail	(0.3)
Utilities	5.6	Oil & Gas Equipment & Services	(1.0)
Communication Services	5.1	Leisure Products	(1.2)
Real Estate**	5.1	Oil & Gas Exploration & Production	(1.5)
Materials	4.3	Environmental & Facilities Services	(1.5)
Energy	2.6	Casinos & Gaming	(1.6)
Positive Sectors:	**100%**	**Positive Sub-Industries:**	**92%**

Source: CFRA, S&P DJ Indices. *12/31/89-12/31/22. **Since 2016.

SUB-INDUSTRY OUTLOOK

Financial Exchanges & Data

Outlook: Positive

Alexander Yokum, CFA
CFRA
Equity Analyst

We have a positive fundamental outlook on the financial exchanges & data sub-industry for the next 12 months. As a group, the major U.S. exchanges have grown EPS at nearly double the speed of the S&P 500 over last decade and, impressively, were able to grow before, during, and after the pandemic. With rapid innovation in the exchange space, we expect most exchanges to continue to grow EPS at a quick pace as they meet client needs with new products and services.

Following elevated trading volumes in 2022, we expect financial markets to remain choppy in 2023, but we see Y/Y comparisons as relatively difficult given tough comps. Outside of reliable recurring revenue, exchanges offer a market hedge with economic uncertainty increasing the attractiveness of transaction-related exchange products.

We expect a falling rate per contract (RPC) to pressure exchanges that heavily rely on trading volumes. For years, heavy competition in the exchange space has led to a decline in the average RPC across trading products. As a result, increases in revenue from higher trading volume is continually hindered by a falling RPC. Our expectation is that this trend will largely continue across all exchanges and relying on non-proprietary trading products will lead to underperformance in the long term.

Regulation could increase equity trading volumes at stock exchanges given 40%+ of trading occurs off exchange. For years, exchanges have seen volumes move off-exchange to dark pools in a trend that, until recently, seemed inevitable to continue. In fact, since 2011, off-exchange volumes have increased from 30% to 42% of total equity trading volume. However, the SEC has begun talks on reforming equity markets as it looks to focus on transparency around best execution, disclosure of execution quality, and a general levelling of the playing field between exchanges and dark pools.

Data providers, largely the ratings agencies, struggled in 2022 as geopolitical uncertainty, slowing economic growth, and a hawkish Federal Reserve severely impacted debt issuance volumes. Many corporations were coming from a position of power as they pulled forward debt issuance in 2020 to take advantage of historically low interest rates. As a result, corporations have sat on the sidelines when possible, resulting in corporate debt-to-GDP levels falling from a high of 57% in Q2 2020 to under 49% as of Q4 2022. However, we see 2022 as a low watermark for debt issuance and expect issuance levels to rise in 2H 2023 as the extreme uncertainty of 2022 and early 2023 moderates. We see issuance momentum continuing through 2025 as a growing level of corporate rated debt matures and needs to be replaced. Thus, we expect credit ratings agencies to see improving performance as cost-cutting measures are met with improving debt issuance conditions. An added benefit should come from the analytics businesses, which help smooth out transaction-related revenues, given the acyclical nature of analytics revenue.

Year-to-date through June 16, 2023, the S&P Composite 1500 Financial Exchanges & Data Index was up 10.9%, compared to the S&P Composite 1500 Index up 14.1%. For the full-year 2022, the sub-industry fell 25.2%, compared to the S&P 1500 down 19.1%.

The table below lists the U.S.-based 4- and 5-STARS rated companies in the financial exchanges & data sub-industry. ■

RECOMMENDED STOCKS IN THE FINANCIAL EXCHANGES & DATA SUB-INDUSTRY

COMPANY NAME / SYMBOL	STARS	RECENT PRICE ($)	12-MONTH TARGET PRICE ($)	SPGMI'S QUALITY RANKING	MARKET CAP ($B)	P/E*
FactSet Research Systems Inc. / FDS	4	404	475	A	16.22	24.6
Intercontinental Exchange Inc. / ICE	4	111	130	A-	62.26	18.1
Moody's Corporation / MCO	4	336	380	A-	62.12	29.8
Nasdaq Inc. / NDAQ	5	50	76	B+	24.81	15.8
S&P Global Inc. / SPGI	4	388	435	NR	124.82	26.8

Source: CFRA. *Based on 2024 EPS estimates.

THEMATIC RESEARCH

Large U.S. Banks

Cracks in commercial real estate

Kenneth Leon
CFRA
Equity Analyst

The size of the U.S. commercial real estate (CRE) market is enormous. The National Association of Real Estate Investment Trusts (Nareit) did a study back in 2021 that quantifies CRE at $20.7 trillion. The U.S. banking industry had $2.4 trillion in total loans outstanding at the end of 2022, spread between different areas of CRE property types and activities. As of Q1 2023, large banks were 30% of CRE total loans, mid-size banks 49%, and small banks 21%. Our focus is on the largest U.S. banks, which showed a net charge-off rate of 0.09% and a nonperforming loss (NPL) formation of 0.54%, compared to 0.17% for all banks. These ratios are expected to deteriorate further in 2H 2023 with a weaker U.S. economy. Nonetheless, where we are today on total CRE delinquencies is still below the pre-pandemic level (0.95% in Q1 2023 versus 1.01% in Q1 2020).

We don't see systemic risk from CRE loan exposure, but the office market has weakened since the pandemic. On June 14, WFC stated at an investor conference that it would add $1.0 billion in Q2 2023 to its CRE loan reserves, mostly for offices from $650 million booked in Q1 2023. The bank hopes this helps to get ahead of things with a potentially deteriorating office market. The CFO said, "it doesn't mean you lose money," which we think means market conditions may abate as one possible scenario, with possibly lower rates in 2H 2024.

We are likely to see headline risks to individual office defaults on loans. In late April 2023, Brookfield Asset Management realized loan defaults on two of six office buildings, including a retail center in Los Angeles known as Brookfield DTLA Fund Office Trust Investor Inc. Further risk of foreclosure has risen for the rest of this office portfolio. Problems start here with floating-rate loans that have shorter terms than fixed-rate mortgages. Brookfield DTLA Fund Office Trust Investor is exposed to $2.3 billion in floating interest rate loans that mature in 2023 and 2024. The result is trying to refinance CRE loans with significantly higher mortgage rates that make the property no longer economic with weakened office fundamentals – lower building values due to low leasing absorption, higher vacancies, more lease incentives, and lower rental rates.

Landlords with floating rate debt are pushed into a corner with few choices, in our view. The cost of hedges against floating rate loans have surged to levels that changed the investment model for certain offices. Lenders in the commercial mortgage-backed securities (CMBS) market and banks do require borrowers to hedge their interest rate risk when they have variable or floating rate loans. The share of floating rate loans in total CMBS issuance is around 60%, according to Trepp data. This compares to right before the 2007-2008 financial crisis, when floating rate loans were below 15%.

Unlike past economic cycles, the decline of office real estate values is linked to negative secular trends. The pandemic has shifted to full-time remote work or hybrid models that require less office space than before. We believe these factors lead to not making enough money to support expected debt payments, leasing costs, and other operating expenses. As the mortgage refinancing story plays out in 2023-2025, we will likely see higher delinquency rates on CRE loans, especially on office properties financed previously with floating rate debt that requires refinancing. Property owners looking to unload troubled offices find the transaction market very weak. In Q1 2023, office sales markets declined 68% to $10.7 billion, according to MSCI Real Assets. Select office transactions are going for steep discounts compared to values in 2019. A major office tower at 350 California St. in San Francisco went for $60 million, or 80% below its previous

(Continued on page 4)

NEGATIVE IMPLICATIONS

COMPANY / TICKER	STARS	RECENT PRICE ($)	TARGET PRICE ($)	MARKET CAP ($B)
Bank of America Corp. / BAC	4	28	41	227.68
Citigroup Inc. / C	3	47	53	92.30
JPMorgan Chase & Co. / JPM	4	140	160	415.90
Wells Fargo & Company / WFC	4	41	50	156.28

Source: CFRA.

THEMATIC RESEARCH

Large U.S. Banks

(Continued from page 3)

valuation of $300 million.

Commercial mortgage loans are important even though they are not one of the largest areas of loan activity. WFC's commercial mortgage loans outstanding represented 16.3% of total loans at the end of Q1 2023, followed by JPM at 11.3%, BAC at 7.0%, and C at 3.6%. However, commercial mortgage loans may have higher credit risk exposure to higher interest rates with variable rate debt and maturities leading to mortgage refinancing.

What we know about CRE is that there are long lead times to changing market conditions and property types that might be higher credit risk exposures, such as office real estate. Historically, overall CRE suffers when we experience a severe and prolonged recession, such as the Great Recession that started in December 2007 and ended in June 2009, or over 18 months' duration. For office real estate, overbuilding and elevated rental rates can lead to market downturns, as we saw in 2001 through 2005 following the tech boom period in 1999 and 2000. On the development side, where construction loans are provided by lenders, there can be long lag times between getting building permits and the final completion of office properties. In some cases, the construction period can extend through an entire economic cycle. Thus, CRE can be risky for banks.

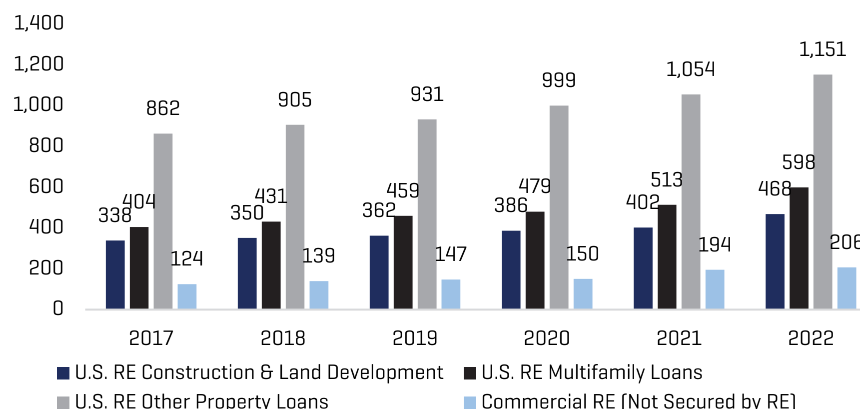
Large U.S. banks have CRE loan exposure, but not significant relative to total loans outstanding. We think the most sensitive categories to loan delinquencies and loan default are construction and land development as well as CRE (not secured by real estate). In our opinion, U.S. real estate multifamily loans are relatively stable, with a housing shortage and affordability pressures on households that are squeezed out of home ownership. We are only seeing some multifamily pressure in Sun Belt markets, where new supply continues to come to market. Over time, we do not see this leading to a market downturn as the U.S. population migrating to the Southeast and Southwest regions serves as a release valve of any supply pressure.

We would point out that the large U.S. banks have diversified CRE loan portfolios, including industrial, multifamily, office, self-storage, hotels leisure, and specialized markets like data centers and wireless towers. Estimated property values, or net asset values (NAV), are an important metric for bank lending, which becomes more challenging when there is a significant decline in real estate transactions as we now see in the office market and less so in the overall CRE market.

CRE loan underwriting is more challenging today. To get funding, we are seeing higher risk with a shift to full interest-only commercial mortgages in response to a 200-bp rise in interest rates. Loan-to-value has also deteriorated to 59.90% in Q1 2023 from 65.00%, or 590 bps lower, since Q1 2020. Cap rates are more difficult to summarize since the volume of CRE transactions has significantly declined in the past year. Generally, high cap rates indicate greater perceived risk and lower-than-average net operating income growth prospects. In our opinion, most of the key underwriting measures are likely to show further deterioration in the next 12 months with the Fed in either a rate rise or rate pause regime. Only when we begin to see the Fed move to a rate cut regime

(Continued on page 5)

U.S. BANKS – COMMERCIAL REAL ESTATE LOAN COMPOSITION*



Source: S&P Global Market Intelligence, as of December 31, 2022. *$ Billion.

THEMATIC RESEARCH

Large U.S. Banks (Continued from page 4)

can we see the benefits to CRE underwriting measures and the underlying net asset values for properties, in our view.

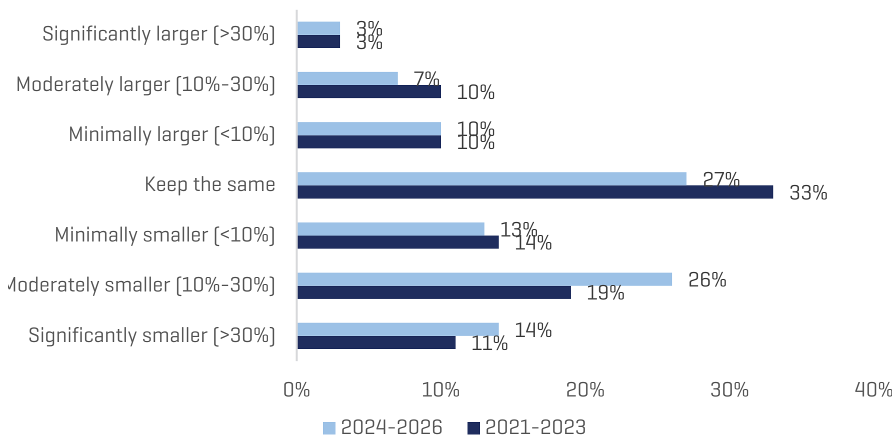
Current surveys of the office real estate market are gloomy. From a CBRE survey, primary tenants are expected to reduce their future office space from 2023 through 2026. In some cases, respondents are planning to significantly move to smaller offices (greater than 30% reduction). Downsizing is most prominent among technology and financial services companies with 64% reporting a reduction in their office space in the past three years. Nearly 70% of the pressure of future downsizing of total office space is coming from the larger tenants. We think landlords have no choice but to renegotiate existing leases to benefit large anchor tenants. For those primary tenants facing locked-in long-term leases, we are seeing significant increases in subleasing excess space. CBRE says the subleasing market is saturated depending on size, location, and remaining lease term.

Office real estate has deteriorated further in 2023. CBRE's review in Q1 2023 shows office job growth has risen, but office demand further weakened with 16.5 million sq. ft. of negative net absorption – the weakest quarter for office demand in two years. There were exceptions in the Sun Belt markets like Charlotte, Dallas/Fort Worth, Miami, and Nashville. CBRE stated that negative net absorption, along with new supply of 5.4 million sq. ft. of new office space, pushed the office vacancy rate up by 50 bps Q/Q to 17.8% for the U.S. office market. In Q1 2023, leasing activity slowed by 25% Q/Q and 35% Y/Y. Sublease availability grew by 12.4 million sq. ft. to a record high of 189 million sq. ft. for the office market. Vacancies by metro market were highest in Fairfield County, Connecticut (25.5%); Columbus, Ohio (25.0%); Chicago (24.2%); Dallas/Fort Worth (24.3%); Atlanta (23.7%); Houston (23.6%); and Phoenix (23.6%). Employment growth exceeded the U.S. average in New York City, Boston, and Los Angeles.

The economic scenario of a prolonged and severe recession will turn against the large banks on CRE credit loan exposure. We think a short and shallow recession bodes well for CRE overall credit risk, except for office buildings. This property type already faces a secular downturn, with changes to hybrid and remote work from full time in the office. Employers with large property holdings as primary tenants are trying to push back against new work arrangements, but the U.S. unemployment rate is low and job openings remain elevated for many industries. The exception may be technology and venture capital firms, especially on the West Coast, but we think the largest technology companies are reducing their real estate footprint.

Our negative implications from cracks in CRE may prove wrong if we see the Fed move to a rate cut regime. On June 14, the Fed's FOMC decided to maintain the target range for the federal funds rate at 5.00% to 5.25%. Holding the target range steady allows the Committee to access data on the U.S. economy. We think the FOMC will raise rates to 5.25% to 5.50% in its July 26-27 meeting, given inflation remains elevated well above the Fed's 2.0% objective. In our opinion, we may see a rate pause well into 2024, which means CRE credit loss exposure may still play out, especially for coastal office buildings that need commercial mortgage refinancing. ■

REAL ESTATE OFFICE PORTFOLIO NEEDS ARE LESS, NOT MORE*



Source: CBRE Research. *CBRE Survey (April 2023).

High-Quality Capital Appreciation Portfolio

To enter the High-Quality Capital Appreciation Model Portfolio, a stock must have an S&P Global Market Intelligence Quality Ranking of A- or better, which indicates a 10-year history of above-average earnings and dividend growth. Stocks must have a 4-STARS or 5-STARS ranking to enter this model portfolio.

CFRA's Senior Portfolio Group may replace any stock in the model portfolio with another stock at any time for reasons that can include a downgrade in STARS or Quality Ranking of the constituents or for other factors.

This model portfolio was launched on May 23, 2003. For the 10-year period ended May 31, 2023, the model portfolio rose at an average annualized rate of 12.60%, outperforming the benchmark S&P 500 Equal Weight Index's 11.10% gain for that period. For 2022, the model portfolio saw a 7.94% loss, outperforming the equal-weighted benchmark's 11.95% loss. Past performance is no guarantee of future results. ■

HIGH-QUALITY CAPITAL APPRECIATION PORTFOLIO

SYMBOL	COMPANY NAME	ENTRY DATE	ENTRY PRICE ($)	RECENT PRICE ($)	12-MONTH TARGET PRICE ($)	STARS	SPGMI'S QUALITY RANKING
AAPL	Apple Inc.	2/8/2021	135.71	187	190	4	A+
BALL	Ball Corporation	12/4/2020	92.65	56	72	5	A-
BLK	BlackRock Inc.	11/11/2019	452.61	679	805	5	A
CMCSA	Comcast Corporation	5/13/2019	39.20	41	50	4	A-
CVS	CVS Health Corporation	3/18/2019	51.35	69	75	3	A-
MSFT	Microsoft Corporation	8/3/2020	212.28	340	370	5	A
NOC	Northrop Grumman Corporation	3/9/2020	300.41	458	454	3	A
RTX	Raytheon Technologies Corporation	10/10/2016	51.08	97	118	4	B+
SCHW	The Charles Schwab Corporation	7/29/2019	41.77	53	66	5	A
PG	The Procter & Gamble Company	10/10/2022	123.76	150	154	3	A-
TJX	The TJX Companies Inc.	1/11/2022	73.20	81	80	3	A-
DIS	The Walt Disney Company	11/14/2011	31.81	88	127	4	A
TMO	Thermo Fisher Scientific Inc.	3/19/2018	209.42	528	550	3	A+
UNH	UnitedHealth Group Incorporated	12/17/2018	243.84	479	595	4	A+
V	Visa Inc.	1/14/2019	133.85	228	272	4	A+

Source: CFRA.

Portfolio Focus: Microsoft Corporation

Microsoft's (MSFT) products include operating systems, cross-device productivity and collaboration applications, server applications, business solution applications, desktop and server management tools, software development tools, and video games. The company also designs and sells devices, including PCs, tablets, gaming and entertainment consoles, other intelligent devices, and related accessories.

Our Strong Buy rating is primarily based on MSFT's ongoing and, so far, very successful cloud transition, with strong traction for cloud versions of Office, Dynamics, Teams, and, of course, Azure infrastructure cloud services. Revenue from all "cloud-based" businesses also includes LinkedIn, Bing, and Xbox Live and is now about 65% of total revenue. We believe that MSFT will reap greater scale efficiencies through greater cloud adoption while cost cuts are aiding margins/EPS, but greater compute intensity will keep capex spend elevated. Greater revenue potential from AI initiatives and product integration could also support multiple expansion. In addition to ChatGPT, we like opportunities in AR/VR for gaming and a growing number of industrial use cases well-suited to HoloLens goggles and the development platform.

Our 12-month target price of $370 is based on a P/E of 30x our FY 2025 view, near MSFT's three- and five-year historical forward averages.

We see lower downside risk (in both probability and magnitude) for MSFT vs. many of its faster growing peers, especially given MSFT's very strong balance sheet, which provides more downside cushion than most large-cap stocks in any sector, in our view. *(Angelo Zino, CFA)* ■

Platinum Model Portfolio

The Platinum Model Portfolio combines the top ranked stocks from the Fair Value quantitative ranking system with those from the CFRA STock Appreciation Ranking System (STARS), a qualitative stock selection methodology.

For a stock to enter the Platinum model portfolio, it must carry both a STARS ranking of 5 and a Fair Value Ranking of 5. Stocks are held in the model portfolio for as long as they carry a 5 ranking in at least one system and a ranking of at least 1 in the other system. Due to short-term data issues, a stock may temporarily lose its Fair Value ranking. To reduce turnover in the model portfolio, a stock must lose its Fair Value ranking for two consecutive weeks before it is dropped from the model portfolio. However, if a stock is dropped from STARS coverage, it is immediately dropped from the Platinum Model Portfolio.

In both ranking systems, stocks are ranked in five tiers.

A 5-STARS ranking indicates the relevant CFRA equity analyst expects the total return for this stock to outperform the total return of the S&P 500 Index by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

Meanwhile, a Fair Value ranking of 5 indicates the stock is significantly undervalued compared with the Fair Value universe. The Fair Value model calculates a stock's weekly Fair Value — the price at which a stock should trade given current market levels — using data such as corporate earnings, price-to-book value, return on equity, and current yield relative to the "500."

The model portfolio was launched on July 28, 1995. For the 10-year period ended May 31, 2023, the portfolio posted an average annual gain of 9.64%, slightly underperforming the S&P 500 Equal Weight Index's 10.15%.

In 2022, the portfolio was down 17.17% vs. a loss of 11.95% for the S&P 500 Equal Weight Index.

In 2021, the model portfolio gained 37.62%, beating the 28.98% rise for the S&P 500 Equal Weight Index.

Performance calculations do not account for capital gains taxes, brokerage commissions, and fees — or timing differences between the model and actual investor purchases. Past performance of the model portfolio is not a reliable indicator of potential future results. ■

PLATINUM MODEL PORTFOLIO

SYMBOL	COMPANY NAME	RECENT PRICE ($)	STARS	FAIR VALUE
AER	AerCap Holdings N.V.	62	5	5
ALK	Alaska Air Group Inc.	50	5	3
ALGT	Allegiant Travel Company	122	3	5
ACGL	Arch Capital Group Ltd.	73	5	4
AN	AutoNation Inc.	153	5	5
BWA	BorgWarner Inc.	46	5	4
CLF	Cleveland-Cliffs Inc.	16	5	2
CPRT	Copart Inc.	89	5	3
DAL	Delta Air Lines Inc.	43	5	5
EWBC	East West Bancorp Inc.	50	5	5
EOG	EOG Resources Inc.	108	5	1
FCX	Freeport-McMoRan Inc.	40	5	1
HOG	Harley-Davidson Inc.	34	5	5
KLAC	KLA Corporation	467	5	3
LEN	Lennar Corporation	121	3	5
MTH	Meritage Homes Corporation	135	3	5
MP	MP Materials Corp.	22	5	4
OLN	Olin Corporation	48	5	5
RHI	Robert Half International Inc.	71	5	5
CRM	Salesforce Inc.	213	5	1
GS	The Goldman Sachs Group	320	5	4
GT	The Goodyear Tire & Rubber	13	5	4
UAL	United Airlines Holdings Inc.	53	3	5

Source: CFRA.

The Intelligencer

Headlines, Highlights, and What's on Our Minds

FEDEX REMAINS FOCUSED ON COST CONTROLS: CFRA keeps Hold opinion on shares of FedEx Corporation (FDX 233 ***). Our 12-month target price of $237, up $12, reflects a 10.5x multiple of our FY 2025 (May) EPS estimate, slightly below FDX's historical forward average. We lift our FY 2024 (May) EPS estimate by $0.43 to $17.71 and start FY 2025's at $22.57. FDX reported May-Q EPS of $4.94 vs. $6.87, beating the consensus view by $0.07. Demand was a headwind in Q4, with revenues down 10% Y/Y and volumes lower as well. FDX remains focused on cost controls heading into FY 2024, which makes sense, in our view. We think a struggling consumer will make it difficult for volumes to recover in the near term, and the threat of recession (even if not our base case) would exacerbate the volume issue, should it occur. However, in the longer term, we think FDX's efforts to obtain sustainable cost improvements set the stage for a better FY 2025. The key for investors in the near term (at least for things that are under FDX's control) is execution on its cost program and awaiting the eventual positive inflection point on the economy. *(Stewart Glickman, CFA)*

KB HOME PIVOTS TO SPEC STARTS: CFRA raises opinion to Buy from Hold on shares of KB Home (KBH 52 ****). We lift our 12-month target by $20 to $61, 8.5x our FY 2024 (Nov.) EPS view of $7.21 (up by $1.41; FY 23's up by $0.77 to $6.32), a premium to the five-year forward P/E average. FQ2 (May) EPS of $1.94 beat by $0.62 on revenues of $1.8 billion, $342 million above consensus. Home deliveries increased 6% Y/Y, while average selling prices declined 3%. We see revenue of $6.15 billion in FY 2023 and $6.44 billion in FY 2024 vs. FY 2022's $6.9 billion supported by a Q/Q backlog increase of 4% to $3.4 billion and a tapering of cancellations to 21.8% from FQ1's 36%. Gross margins declined 400 bps Y/Y to 21.4% and operating margins declined 370 bps to 11.7%. The FQ3 gross margin is expected to decline to a trough. The FY 2023 revenue guide is lifted by $450 million to $6 billion (midpoint) supported by cycle time improvement. KBH will pivot to spec starts as it reloads its built-to-order pipeline, which we view favorably due to a tight resale market. FQ2 net orders by region were West Coast +19% Y/Y (33% of total orders), Southwest +10% (20%), Central -19% (26%), and Southeast flat (20%). *(Ana Garcia)*

LIVE NATION ENTERTAINMENT SEES RECOVERY: CFRA reiterates Buy rating on shares of Live Nation Entertainment, Inc. (LYV 89 ****). We also raise our target by $5 to $100, a forward TEV/EBITDA of 13.5x, below the five-year historical average at 57.9x. We keep our EPS estimates at $1.00 in 2023 and $1.85 in 2024, above consensus estimates at $0.69 and $1.58. We assume a breakout in consumers shifting spending to live event experiences versus buying goods. LYV has seen no pullback in ticket demand and no economic headwinds with results, as ticket holders plan to attend live events. Recovery is underway for LYV and we forecast revenue of $19.3 billion in 2023 and $20.1 billion in 2024 versus $16.7 billion in 2022, following a Covid-restricted $6.3 billion in 2021. In Q1 2023, revenue of $3.1 billion beat consensus by 38%. Corporate sponsorship revenue for 2023 is +47% Y/Y, showing commitments with LYV events. Stadium attendance grew 4x to 3.3 million fans in Q1 2023, up from 800 thousand fans a year ago. This growth primarily came from APAC and Latin America. LYV proposed transparency in the ticketing market with the launch of the Fair Ticketing Act, which makes selling spec tickets illegal. *(Kenneth Leon)*

The Outlook

EQUITY & FUND RESEARCH SERVICES

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EVALUATION SYMBOLS

STARS Rankings

CFRA's evaluation of the 12-month potential of stocks is indicated by STARS:

★★★★★ **Strong Buy**—Total return is expected to outperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

★★★★ **Buy**—Total return is expected to outperform the total return of a relevant benchmark over the coming 12 months.

★★★ **Hold**—Total return is expected to closely approximate the total return of a relevant benchmark over the coming 12 months.

★★ **Sell**—Total return is expected to underperform the total return of a relevant benchmark over the coming 12 months.

★ **Strong Sell**—Total return is expected to underperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares falling in price on an absolute basis.

NR Not Ranked

S&P Global Market Intelligence's Quality Rank

S&P Global Market Intelligence's appraisals of the growth and stability of earnings and dividends over the past 10 years for STARS and other companies are indicated by Quality Rankings:

A+	Highest	**B+**	Average	**C**	Lowest
A	High	**B**	Below Avg.	**D**	In reorganization
A-	Above Avg.	**B-**	Lower	**NR**	Not Ranked

Quality Rankings are not intended to predict stock price movements.