Weekend Thoughts 8/20/22

- Information Technology
    - Analog Devices (ADI)
        - “on pricing increases, I believe that we are in the post-Moore's Law era and in a period of sustained structural inflation in this business for many, many years ahead. I think it's true to say that supply -- we've been increasing, of course. We've invested strongly in our own manufacturing capabilities to be able to secure supply and increase supply actually across the 4 wafer fabs inside ADI. So yes, supply is improving there. And thematically as well as supply has been improving actually right through the pandemic, right over the last couple of years from our subcontractors as well. So I think there is a lightening of supply across the board.”
    - Applied Materials (AMAT)
        - “global supply chains remain stretched. Demand for Applied's products is still higher than our ability to fulfill it, and our backlog continues to grow.”
        - “They're seeing softness in consumer-centric markets, which are being impacted by macroeconomic factors. Auto and industrial demand continues to be solid because those investments are driven by large inflections, such as electric vehicles and industrial automation. In these areas, chip makers are securing long-term capacity agreements that underpin their capital spending plans. While it's too early to provide a forecast for 2023, we believe our business will be more resilient than in the past if there is a demand pullback in certain areas of the market. We expect Applied to remain supply-constrained for the next several quarters.”
        - “As a result, we are slowing down hiring while ensuring we fully fund the R&D programs and strategic operational capabilities that support our long-term growth. Regionalization of supply chains is also something new for the industry. We expect this will provide a small positive tailwind for overall wafer fab equipment spending starting in late 2023.”
        - “The changing macroeconomic environment is causing some customers to adjust the timing of their investments. However, we're confident that our business will be more resilient, thanks to strong pull for a uniquely enabling technology, our large backlog, longer-term visibility from our customers and industry-wide investment in strategic regional capacity. Our long-term view of the market remains unchanged as multiple parallel secular trends drive the semiconductor and wafer fab equipment markets structurally higher.”
        - “you talked about 10, 11 years. If you go back over that time period, we, I think, close to doubled our percentage of subscription agreements versus transactional. So certainly -- and we've increased the length of those agreements to 2.5 years. So that percentage of agreements being so much higher, and it's still growing, that makes that business more resilient.”
    - Cisco Systems (CSCO)
        - “We continue to see strong customer adoption of our software and subscriptions, driven by the targeted investments we've been making.”
        - “There are currently more technology transitions occurring concurrently than I've seen in 20 years. long-term megatrends like hybrid cloud, hybrid work, security, IoT,

400 gig and beyond, 5G and WiFi 6 as well as the move towards application observability will likely provide tailwinds to our growth"
    - "we haven't seen a material demand signal change as we've entered into Q1."
    - "I believe that post pandemic, the view of technology by our customers is much different than it would have been 7, 8, 9 years ago there. I think if you ask our customers if they would pause spending during a crisis, they would probably respond, when is there not going to be a crisis given what we've dealt with the last 3 years?"
    - "In some cases, customers are looking for a little shorter ROI, so that affects how they think about what products they're buying in these kinds of times."
    - "I've been asked if our M&A strategy has changed because of the valuations. And I've said that our strategy hasn't changed, but the openness to talk to us from some of the companies that thought they had different strategic exits might have changed. And so we haven't changed our strategy. We just think that it potentially creates more opportunity for us with companies that might not have been willing because they thought there was a high-flying IPO ahead of them that they may not believe is the case right now. And the market is obviously taking a much different view on profitability versus just growth"
    - "Number one, the pandemic revealed the impact of not keeping your core infrastructure technology up to speed. Customers struggled, and I think it made them realize that they had a lot of tech debt that needed to be dealt with. And they don't want to get in that position again. So that's the first thing. But the second thing is all of these mega trends that I mentioned in my opening comments, I mean, these customers are rearchitecting their entire infrastructure for the first time in years to deal with hybrid cloud and to deal with all of the mobile workers. We see IoT exploding. You see all of the climate activity is going to be a tailwind to our business because you have to connect all these industrial systems to be able to control them. You've got to shift to 400 gig. I mean let me just give -- I'll give you a data point, 400 gig ports we're up almost 700% year-over-year for us. We've got over 1,000 customers now that have bought 400 gig, and we shipped our first 800 gig. So it's just all these trends continue, you got 5G, you've got WiFi 6. You've got this application observability, the rearchitecture of applications. So I think it's a combination of the realization the pandemic brought on around technology debt and never letting them get to that point, and then these mega trends that are going on."
- Health Care
  - Agilent Technologies (A)
    - "We continue to have very, very low order cancellation rates."
- Consumer Discretionary
  - BJ's Wholesale Club (BJ)
    - "We are still seeing some of the things that we talked about in the first quarter where lower -- numbers in the lower end of the economic spectrum, we're seeing a little bit of a pullback there, really not in their traffic so much, but in their overall shopping given they have less government aid dollars than they had in the past. They are still coming to see us in good amounts. Their traffic is fine."
  - Foot Locker (FL)
    - "The consumer is undoubtedly under pressure, especially at the lower end income range, which we began to see in our business as we progressed through the

quarter.”

    - “After a strong start in May, we saw trends slow in June, which continued through mid-July. As trends soften, the promotional environment has become more intense, especially in apparel, but also in footwear. In the back half of July, trends started to pick up meaningfully, especially in our earliest back-to-school markets.”
    - “And we then finished May stronger than we had originally planned. But into June, we saw a slowdown versus our expectations in traffic amid the rapid uptick in inflation, especially in the U.S. Although more dramatic in our lower income customer base, the softening was across the board. That more pronounced softening in our lower income customer base was a trend we saw in our core business as well as our customer segments at WSS. That trend continued into the first half of July. But the back half of July began to improve, particularly in the early back-to-school markets. While the back-to school trends are very encouraging, given the uncertainty in the macroeconomic environment, we are still tempering our expectations for the balance of the year.”
    - “Based upon our current visibility, we expect these macro headwinds to put pressure on consumer spending through the back half of the year. As such, we now expect to achieve the lower end of our original comp and earnings guidance.”
- The Home Depot (HD)
    - “both Pro and DIY sales growth was positive with Pro outpacing DIY. We're encouraged by the continued momentum we are seeing with our Pros and they tell us their backlogs remain healthy”
    - “We find ourselves in a unique environment with many crosscurrents. We're operating in a broad-based inflationary environment not seen in 4 decades while managing through constrained global supply chain conditions, all against the backdrop of monetary policy shifts intended to moderate demand. We also see engaged and resilient homeowners who have strong balance sheets, consumers spending more time in their homes and continued structural support for home improvement project demand.”
    - “We have not seen that yet. In fact, with the strong performance this quarter, the variability across our regions has been the lowest in markets, has been the lowest that we've seen in some time. So we all appreciate the headlines and follow those very closely. But we have not seen anything in our business yet from macro housing.”
    - “when you think of the wealth that our core customers and their home equity up $9-odd billion, the excess savings rates, the strong jobs and earnings growth of wages and the fact that we're just continuing to spend more time at home in general, people are still super engaged in improving that home that they're spending more time in. So we're certainly benefiting from that longer-term dynamic.”
    - “So really not seeing any trade down. We've got strength in our ticket above $1,000, and that speaks to the project and to the Pro customer. We will say in categories like grills, mowers, laundry and a few other bigger-ticket items, it's possible there is a price sensitivity. But as Ted commented, there's COVID pull forward, there's stimulus effect.”
- Kohl’s Corporation (KSS)
    - “Our second quarter results reflect a middle-income customer that has become more cost-conscious and is feeling greater pressure on their budgets. Therefore, we

are seeing customers make fewer shopping trips, spend less per transaction and shift towards our value-oriented private brands. We have responded to this dynamic environment, taking action to adjust our plans and adapt to a softer demand outlook. We've increased promotions. We are being aggressive on clearing excess inventory. We are pulling back on receipts. And we are managing expenses diligently. We acknowledge that many others are taking similar actions, which will likely make for a more promotional environment in the near term."

    - "We have taken action to address inventory, including increasing promotions, being aggressive on clearing excess inventory and pulling back on receipts. Given our updated business outlook, we now expect inventory to end the year up high teens as compared to 2021."
    - "all the unpacking we've done with the customer is they're feeling tremendous pressure on their budgets as inflation has taken hold in more essential categories like food and gas, and they're spending less in apparel."
    - "June was our toughest month. So we started with seeing some encouraging spring seasonal selling. Things really fell off in that kind of late May and into June. As we looked at the correlation to the inflationary pressures that was having a massive impact to our business, we took a number of actions in July in terms of driving value. That's clearly what the customer wants, and the customer was responding. So that was encouraging. And we recognize that the environment is going to be promotional. It's going to be very value-driven."
    - "And this is our second quarter where our private brands actually outperformed our national brands. So all of those things, again, point to a customer that is under a lot of financial pressure and so we have to make sure we're showing up in a relevant way. But clearly, and what we saw in the second quarter is, fewer trips and less in their basket. It's important to note, as we made comments in the remarks, that we're seeing this largely in our middle-income customers. Interestingly, in our higher-income customers, we're actually seeing more customers, and they're spending more"
- Lowe's Companies (LOW)
    - "Also, while we plan for a modest sector pullback this year as we lap outsized DIY consumer demand, we now believe that certain categories like patio and grills are disproportionately impacted by the unprecedented demand from 2020 and 2021. This unprecedented demand was likely fueled by the combination of 3 rounds of government stimulus, an increase in consumer savings rate and a temporary shift away from spending on services towards spending on goods, including home improvement products"
    - "At this point, we are not seeing indications of material trade down. If anything, we're seeing the opposite with continued strong demand for our new and innovative products at higher price points."
    - "the market dynamics that pressure the home builder are not necessarily the same market dynamics that pressure the home improvement retailer. At Lowe's, the 3 highest correlating factors of home improvement demand are home price appreciation, the age of the housing stock and disposable personal income."
    - "Another interesting trend from the quarter is the ongoing demand for innovation, reflecting underlying consumer strength. Rather than seeing trade down, in many cases, we are seeing customers trade up, spending more to purchase the latest technology like battery-powered products"

    - "And as raw materials down, we're positioned and prepared to renegotiate prices with our suppliers. We're actually very much underway in certain areas with Bill and his team. And then from a pricing perspective, like we always do, we're going to leverage a portfolio approach if and when we call back the dollars, but we're always going to ensure that we're going to be competitive there as we approach pricing."
- Ross Stores (ROST)
    - "On the consumer, we're not seeing any change, certainly. Since -- if I take the first to the second quarter with our comps, they've been relatively consistent. The composition of comps have been relatively consistent. If I compare it to when we started to lap the stimulus from last year, and our customer surveys and our own performance would suggest that where we're really seeing pressure is the lower-end consumer. But on the trade-down customer, there's no indication that is in our data that would suggest that that's happening."
- Target Corporation (TGT)
    - "we've meaningfully reduced our ownership and commitments in categories where we've seen softening demand."
    - "What we're seeing in our results and hearing from our guests is that they still have spending power, but they're increasingly feeling the impact of inflation. And while the recent reduction in prices at the gas pump has been encouraging, guest confidence in their personal finances continues to wane. Against that backdrop we've seen our guests shop our owned brands in bigger ways and more frequently knowing they are choosing great quality products with incredible value. We've also seen guest behavior evolve as they focus on optimizing their personal budgets through a heightened response to promotions as well as greater trip consolidation."
    - "And today, while conditions remain far from what we would have considered normal in the years before the pandemic, there are early signs that both costs and volatility may have peaked. More specifically, lead times in global shipping have begun to decline. Spot rates to move shipping containers have fallen somewhat. And in light of the reduction in petroleum prices we've all seen recently, fuel surcharges have been easing somewhat compared with the peak rates we saw earlier in the second quarter"
- The TJX Companies (TJX)
    - "First of all, U.S. customer trend in the quarter, it's moved around a bit. I think what happened in this quarter is when a little bit of that fuel spike, if you remember back in the middle of the quarter, that's when we had a big ramp-up on that. In addition to really food, those are the 2 inflationary categories that really, we feel, can impact our consumer the most."
    - "There was no -- let me be clear on your question about pushback on the pricing. . . fact, we're measuring our turns and all of these things relative to pre-COVID, fiscal '20, calendar '19. And in most cases, we are actually turning our inventories faster than then. And that, as you know, was a very, very good year for us and a real, actually, model of business that we're very happy with from an inventory turn and sales perspective. So we have 0 concern overall."
    - "So we haven't seen the promotional environment, if anything, because of what's happened with inflation, again, we look at the promotional environment is less promotional. And a lot of these costs are baked in even going forward. I foresee the promotional environment not getting any worse for a few years. I think we're good for a couple of years there."

- Walmart (WMT)
  - “We're pleased to see more families from a variety of income levels choose us as they look for value.”
  - ”As a backdrop, the shifts that we've seen in consumer behavior through the pandemic, shifting from in-store to online, along with big swings in the purchase of goods versus services and then the reversion back to pre-pandemic norms, have been sharp and difficult to predict. These trends have been exacerbated by inflationary pressure on the consumer that many of us have not experienced in our lifetime, the effect of which has recently changed consumption patterns in certain categories for us, notably general merchandise”
  - “We've also canceled billions of dollars in orders to help align inventory levels with expected demand.”
  - “late Q2, early Q3 was traffic count was a bit stronger than what we've seen in the preceding 2 months.”
  - “what have we seen in previous cycles. We did see some pickup in the last cycle, that was a downturn in 2008, '09. But there are a few things that are different now that I think I'd like to point out. And in that time period, we had our store business and a small e-commerce business. We did not have food pickup. We didn't do delivery from stores. We didn't deliver groceries. We did not have Walmart InHome. We didn't have Walmart+. So our ability to serve customers more flexibly -- in a more flexible manner than what we could have 13, 14 years ago was pretty dramatic. So definitely a lot of work to do to ensure that we're taking care of those customers and we're focused every week on satisfaction scores and accuracy of delivery and things like first time pick rate, which is an indicator of did we get your entire order right at the very first time we try to deliver it. Those will all be important in terms of being able to hold on to new customers. But we definitely have a number of ways that we can serve customers today that just, quite frankly, did not exist the last time we went through a downturn.”
- Consumer Staples
  - The Estee Lauder Companies (EL)
    - “We are concerned, however, that the recovery this fiscal year will once again not be a smooth one. Record inflation and the threat of recession or slowdown in many markets could temporarily dampen consumer enthusiasm and is causing some retailers to be more cautious regarding inventories. The strengthening dollar is putting pressure on our international earnings. Additionally, heightened geopolitical tensions could prove to be disruptive. With that backdrop in mind, for the full fiscal year, organic net sales are forecasted to grow 7% to 9%.”
    - “I would say again is we are starting the year with a fair amount of disruption as we just spoke about in some of our very important markets. And we are assuming a more gradual recovery, and that, too, impacts our unit growth.”
- Industrials
  - Deere & Company (DE)
    - “Our order books for the remainder of the current fiscal year are full, and we see signs of robust demand into 2023with some order books already full through the first half of next year.”
    - “End markets for earthmoving are expected to remain strong as oil and gas activities remain steady, U.S. infrastructure spend begins to ramp and CapEx programs from the independent rental companies drive re-fleeting efforts. Housing starts have

moderated though still remain elevated versus historical levels. Additionally, record low levels of new and used equipment will dampen any slowdown."

- "Overall, Financial Services continues to deliver steady results. Credit loss provisions, lease return rates and past dues are all in good shape, reflecting the solid balance sheet for our customers."
- "the environment is supportive of replacement demand especially when you consider that farmers haven't been able to replenish their fleets as much as they wanted to this year. The age of the fleet remains above average. Additionally, dealer inventories remain at historic lows since the industry shorted demand the last couple of years due to supply constraints. These factors should help extend the duration of the replacement cycle."
- "Used inventory across the board for large ag equipment is all-time low. So -- and if you look at how across the board, with lease returns coming back, no one's sending any back. I mean, we're in a really good spot, and we're not going to really build any inventory even through '23."

- Materials
  - BHP Group Limited (BHP)
    - "The realities of climate change remain. The world still needs to decarbonize, and the infrastructure requirements for that are immense. The world's population will continue to grow, urbanize and demand higher standards of living, and that means the demand for our commodities will continue to grow."
- Labor market reads
  - ZipRecruiter (ZIP)
    - "in spite of the strength of the quarter as a whole and the shortage of talent for currently-open job postings, we began to see employers pulling back on job postings during the final weeks of June."
    - "We expect the macroeconomic environment of increasing inflation, rising labor costs and interest rates to have a more pronounced impact on the hiring environment in the second half of 2022."
    - "in the back half of June, we saw a broad-based across all job categories and all seniority levels pull back in the amount of open jobs that – new jobs that were being posted."

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