

Research Portfolios Update

Income & Growth portfolio changes

Portfolio Strategy

We made changes to the Income & Growth portfolio. We are deploying the 2.5% cash from the sale of Boeing (BA). We are increasing our weight in Apple (AAPL) from 7.0% to 8.0%, buying a 1.0% position in both Howmet Aerospace (HWM) and Western Digital (WDC) and reducing our position in Costco (COST) from 4.0% to 3.5%.

Exhibit 1: Income & Growth Portfolio changes

Deploying cash

Portfolio	Sector	Action	Company	Ticker	Investment Rating	Price 1/24/24	Old Position	New Position
I&G	IT	Increase	Information Technology				25.5%	27.5%
		Buy	Western Digital Corp	WDC	C-1-9	\$58.03	0.0%	1.0%
		Increase	Apple Inc	AAPL	B-1-7	\$194.50	7.0%	8.0%
	IND	Increase	Industrials				8.0%	9.0%
		Buy	Howmet Aerospace Inc	HWM	B-1-7	\$56.34	0.0%	1.0%
	CST	Reduce	Consumer Staples				9.5%	9.0%
		Reduce	Costco Wholesale Corp	COST	B-1-7	\$686.51	4.0%	3.5%
	Cash	Reduce	Cash				2.5%	0.0%

Source: BofA Global Research

BofA GLOBAL RESEARCH

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United States

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Western Digital (WDC): Western Digital is a leading developer, manufacturer, and provider of data storage devices and solutions that address the evolving needs of information technology (IT) and the infrastructure that enables the proliferation of data in virtually every industry. The company makes hard disk drives (HDDs) (50% of sales), which record, store, and recall volumes of data, and fast-growing solid-state drives (SSDs), known as flash drives, used in many mobile devices. HDD accounts for a major portion of Western Digital's revenues, although the company also makes devices used in servers, cloud computing data centers, and home entertainment products such as set-top boxes and video game consoles as well as mobile phones. The company sells to manufacturers, retailers, and distributors and generates around half of its revenue from the Asia/Pacific region.

Howmet Aerospace (HWM): Howmet Aerospace, Inc. engages in provision of engineered solutions for the aerospace and transportation industries. It operates through the following segments: Engine Products, Fastening Systems, Engineered Structures, and Forged Wheels. The Engine Products segment produces investment castings, including airfoils, and seamless rolled rings primarily for aircraft engines (aerospace commercial and defense) and industrial gas turbines. The Fastening Systems segment is involved in the production of aerospace fastening systems, as well as commercial transportation fasteners. The Engineered Structures segment includes titanium ingots and mill products for aerospace and defense applications and is vertically integrated to produce titanium forgings, extrusions forming and machining services for airframe, wing, aero-engine, and landing gear components. The Forged Wheels segment provides forged aluminum wheels and related products for heavy-duty trucks, trailers, and buses globally.

Exhibit 2: Income & Growth portfolio

Current holdings and weights

Sectors/Target Weights	Symbol	Proposed Weight	Price	Yield	QRQ Rating
			1/24/2024		
Communication Services (5.5%)					
Netflix	NFLX	2.5%	\$544.87	0.0%	B-1-9
Alphabet A	GOOGL	3.0%	\$148.70	0.0%	B-1-9
Consumer Discretionary (13.5%)					
Amazon.com	AMZN	3.0%	\$156.87	0.0%	B-1-9
Hilton Worldwide	HLT	1.5%	\$187.57	0.3%	B-1-7
O'Reilly Auto	ORLY	1.0%	\$1,018.45	0.0%	B-1-9
Ferrari	RACE	1.5%	\$335.24	0.6%	B-1-7
McDonald's	MCD	2.0%	\$300.44	2.2%	A-2-7
Tesla	TSLA	1.5%	\$207.83	0.0%	C-2-9
Ross Stores	ROST	1.0%	\$138.73	1.0%	B-1-7
The Home Depot	HD	2.0%	\$347.27	2.4%	B-1-7
Consumer Staples (9.0%)					
Costco	COST	3.5%	\$686.51	0.6%	B-1-7
Procter & Gamble	PG	1.0%	\$152.12	2.5%	A-1-7
Kenvue	KVUE	2.0%	\$20.43	3.9%	C-1-7
Walmart	WMT	2.5%	\$160.50	1.4%	A-1-7
Energy (6.0%)					
ExxonMobil	XOM	3.0%	\$99.60	3.8%	B-1-7
Schlumberger	SLB	1.5%	\$51.67	2.1%	C-1-7
ConocoPhillips	COP	1.5%	\$109.67	0.5%	B-1-7
Financials (14.5%)					
Progressive Corp	PGR	2.5%	\$178.36	0.2%	B-1-7
BlackRock, Inc.	BLK	2.5%	\$785.75	2.6%	B-1-7
Visa	V	3.0%	\$271.65	0.8%	B-1-7
JP Morgan Chase	JPM	3.0%	\$170.50	2.5%	B-1-7
SPGI	SPGI	2.5%	\$445.90	0.8%	B-1-7
TD Bank	TD	1.0%	\$60.80	5.0%	B-2-7
Health Care (11.0%)					
Boston Scientific	BSX	2.5%	\$59.92	0.0%	B-1-9
Eli Lilly	LLY	2.0%	\$633.70	0.8%	B-1-7
UnitedHealth Grp	UNH	3.0%	\$513.23	1.5%	B-1-7
Thermo Fisher	TMO	1.0%	\$539.99	0.3%	B-1-7
Zoetis Inc.	ZTS	2.5%	\$186.07	0.9%	B-1-7
Industrials (9.0%)					
Honeywell	HON	1.0%	\$199.87	2.2%	B-1-7
Howmet	HWM	1.0%	\$56.34	0.4%	B-1-7
Union Pacific	UNP	2.5%	\$242.33	2.1%	B-1-7
Parker Hannifin	PH	3.0%	\$464.88	1.3%	B-1-7
United Rentals	URI	1.5%	\$576.90	1.1%	C-1-7
Information Technology (27.5%)					
Apple Inc.	AAPL	8.0%	\$194.50	0.5%	B-1-7
Microsoft	MSFT	8.5%	\$402.56	0.7%	B-1-7
ServiceNow	NOW	2.0%	\$763.42	0.0%	B-1-9
NVIDIA	NVDA	3.5%	\$613.62	0.0%	C-1-7
Amphenol	APH	2.0%	\$100.66	0.9%	B-1-7
Western Digital	WDC	1.0%	\$58.03	0.0%	C-1-9
Palo Alto Networks	PANW	1.0%	\$340.24	0.0%	B-2-9
Broadcom	AVGO	1.5%	\$1,253.87	1.7%	B-1-7
Materials (0.0%)					
Real Estate (4.0%)					
Welltower	WELL	1.5%	\$87.13	2.8%	B-1-7
Prologis, Inc.	PLD	2.5%	\$125.44	2.8%	B-1-7
Utilities (0.0%)					
Cash (0.0%)		0.0%			

Source: BofA Global Research

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Price objective basis & risk

Apple Inc. (AAPL)

Our PO of \$225 is based on approximately 32x our C24E EPS. Our target multiple compares to the 5-year historical range of 16-34x (median 27x). We believe a multiple at the higher end of the historical range is justified given a large cash balance and opportunity to diversify into new end markets, increasing mix and diversity of services.

Downside risks are: a) weaker iPhone 15 cycle on consumer spending risk, b) weaker near-term services trajectory where App Store & Licensing can decelerate, c) gross profit dollars declining y/y next few quarters, d) iPads/Macs reverting to pre-COVID levels, and e) stronger dollar. Other risks are potential trade conflicts, tariffs, longer iPhone replacement cycles, commoditization in the smartphone market, intensifying competition in the tablet market, ability to manage beat and raise expectations for EPS estimates, and requirement to maintain pace of product innovation.

Upside risks are: a) stronger sales of Pro iPhone models which can help average selling price and help the mix of the business, b) est. revisions can be lower vs. peers, c) potential new products (AR/VR), and services (advertising). Other upside risks are stronger than expected iPhone cycle, gross margin upside from better mix of higher end iPhones, tailwinds from lower memory costs, and a faster than expected recovery in emerging markets.

Boeing (BA)

Our PO of \$255 is based on the near-term average FCF of \$15/share and relative discount to the S&P500 of 0.8x (about half standard deviation above historical average). In our view, a multiple roughly in line with the historical average fairly reflects the looming aerospace recovery, strong demand for commercial jets, defense opportunities, and the lack of dividend.

Upside risks to our PO are the possible involvement of an activist shareholder, better-

than-expected cash margins at 787 and/or MAX programs, the company's ability to sustain 777 delivery rates through the bridge to 777X, lower-than-expected 777X, future single-aisle and middle-of-the-market aircraft development costs.

Downside risks to our PO are as follows: Tight competition for engineering talent in the current labor market could make new product development more challenging. Execution risk on new programs and production ramp-ups (737MAX, 777X, KC-46) could result in cost overruns and margin contractions. Changes in trade policy that end in a trade war. A sharp and prolonged surge in oil prices to above \$100/bbl would be negative to aircraft demand. A downturn in commercial aviation, due to an exogenous factor, could adversely affect financial results. As aircraft are priced in USD, an unexpected rapid revaluation in the dollar could significantly affect order activity. Also, a strong dollar could improve Airbus' competitive advantage. 787 fixes could take longer than expected.

Costco Wholesale Corporation (COST)

Our price objective of \$740 is based on 41x our F25E EPS of \$17.90. Costco's long-term (20yr) average two-year forward PE is 24x, with a peak of 41x and a trough of 16x. We view a premium valuation as appropriate given 1) COST's healthy customer traffic growth and strong membership renewal rates, which should continue given our expectation for a further rise in the perceived value of shopping at warehouse clubs and COST's leading warehouse club position from a merchandising, store execution, and private label standpoint, 2) COST's strong same-store sales outlook given strong customer traffic growth, and 3) expected continued strength in COST's International segment, which is generating mid-single-digit %+ comps in local currencies and supports Costco's premium valuation.

Downside risks to our price objective are adverse macro shocks, tariffs, regional dependence on California, food inflation/deflation pressures, foreign exchange risk, challenging membership trends, increased competition, wage increases, gas profit comparisons and the potential for increased unionization of COST's employee base, which could pressure labor expenses.

Howmet Aerospace Inc. (HWM)

Our price objective (PO) of \$60 for HWM is based on a relative P/FCF multiple of 1.5x, resulting in a 29.7x P/FCF multiple. We believe a 1.5x relative multiple, above the 1.1x historical average, fairly reflects the upside of the commercial recovery.

Upside risks to our PO are an accelerated commercial aero upcycle, additional wins from commercial original equipment manufacturers (OEMs) moving away from VSMPO, increased F-35 sales either domestically or internationally, and further pressure on emissions standards, thus benefitting the company's wheels business.

Downside risks are the economic backdrop results in another downturn to the commercial aero cycle that is not offset by the unmet demand of the last few years, F-35 program deliveries decline and the trucking industry sees a significant downturn.

Western Digital Corporation (WDC)

Our PO of \$49 is based on 14x C24E EPS. This multiple is above the HDD/SSD historical average of 9x, which we view as justified as it balances near-term sluggish end markets offset by longer-term improving trajectory of the business both in HDDs and in NAND. WD is a cyclical company. Near-term estimates are lower given lower demand from weaker macro.

Downside risks are: (1) unit declines in desktops and notebooks (2) worse than expected high-capacity HDD industry, (3) faster declines in NAND Flash pricing, (4) higher NAND manufacturing cost from either stronger Yen, or manufacturing yield issues, (5) lower royalty revenue from NAND licensing, (6) degradation of cash position and lower free

cash flow and (7) failure of strategic actions to drive incremental value

Upside risks are: (1) significant pickup in high capacity/nearline HDDs, which could drive ASPs and gross margin higher, (2) share gains in enterprise NAND flash SSDs, (3) consumer PC refresh cycle, (4) improved free cash flow generation and faster debt pay down and (5) strategic options that drive the stock higher.

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