Global Research Highlights

Entering a virtuous cycle

Investment Strategy

15 March 2024

Global

Investment Strategy
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Raising S&P 500 EPS

Savita Subramanian and team raised their 2024 S&P 500 EPS estimate this week to $250 (+12% YoY; vs. $235 previously), the highest top-down forecast on the Street. Companies delivered another strong beat in 4Q and our economists raised their 2024 GDP forecast to +2.7% YoY (vs. +1.4% in November). The 1.3ppt increase in GDP forecast translates to a 5ppt boost to EPS growth, all else equal. 2023 was a transition year for Corporate America, and companies have now adjusted to the new higher rate and tepid demand environment. The team also sees a virtuous cycle forming from Artificial Intelligence (AI) investments with hyperscalers expected to increase capex by 27% YoY in 2024 and productivity gains from AI acting as a tailwind.

AI set be a key driver for server market growth

On the topic of AI, Wamsi Mohan and team report on the impact it's set to have on the server market. From 2006 to 2023, the server market grew revenues at mid-single digit CAGR (5.4%), and units at low-single digit CAGR (2.8). Looking ahead they see AI driving most of the future growth in server revenues over the next 4-years and model the overall server market growing revenues double-digits (about 23% CAGR) between 2023-2027, while server units grow at high-single digits (8.6% CAGR) in the same timeframe. Within their coverage universe, they see Super Micro, DELL, and HPE directly benefiting from higher AI server demand, while NTAP, PSTG, WDC and STX benefit from increased demand for storage driven by increased AI workloads.

A little better inflation picture than January

Our US Economics team reports that the February inflation data were not great but were modestly encouraging after alarming data in January. The details of the PPI report that flow through to the calculation of PCE inflation were generally softer this month than last. Based on the January PPI and CPI data, they expect core PCE inflation to print at a soft 0.3% m/m in January (0.28% unrounded) which is still too high for the Fed. The team continues to expect the beginning of a cutting cycle in June with a 25bp cut but notes the Fed will need to see more improvement in the upcoming inflation data to have enough confidence to begin to ease.

Consumer Conference

Our consumer teams hosted companies and investors at the BofA Consumer and Retail Conference this week. See inside for reports from our Consumer Staples and Restaurants analysts detailing key takeaways.

Top Macro reports

Top Industry reports

Top Stock reports

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Refer to important disclosures on page 18 to 20. Price Objective Basis/Risk on page 13.
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US Watch

February PCE inflation tracking: A small sigh of relief

14 March 2024

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PPI = Producer Price Index

PPI firmer than expected on energy prices

PPI came in firmer than expected in February. Headline rose by 0.6% m/m (expected: 0.3% m/m) owing to a 6.8% increase in gasoline prices. Core increased by 0.3% m/m (expected: 0.2% m/m) and core-core rose by 0.4% m/m (expected: 0.3% m/m). In our view, the data suggests broad-based goods deflation will be harder to come by this year.

Firm core goods but margins are seeing compression

Core goods PPI rose by 0.3% m/m for a second consecutive month in February. This is a touch above the 0.2% m/m run rate in 2022 and was driven by a 0.6% m/m increase in nondurable core consumer goods. On the services side, transportation and warehousing services surged 0.9% m/m owing in large part to a 2.4% jump in passenger transportation. Transportation and warehousing of consumer goods rose by a more modest 0.3% m/m. The good news for the consumer is that firms appear to have absorbed some of these higher costs as margins, trade services PPI, fell 0.3% m/m.

Details for PCE inflation were softer this month

The details of the PPI report that flow through to the calculation of PCE inflation were generally softer this month than last. Monthly changes in PPI physician offices, hospital services, and portfolio management were all weaker in February (Exhibit 7).

Core PCE likely to print at a soft 0.3% m/m in February

Based on the January PPI and CPI (Consumer Price Index) data, we expect core PCE inflation to print at a soft 0.3% m/m in January (0.28% unrounded). Given the PPI data, PCE inflation should slow for financial services financial services (2.5% m/m in Jan vs. 0.5% m/m in Feb); health care PCE (0.5% m/m vs. 0.1% m/m), and core services ex housing services (0.6% m/m vs. 0.3% m/m).

If our forecast proves correct, then the six-month annualized rate of core PCE would likely accelerate from 1.5% to 2.9%, and the y/y rate would remain at 2.8%. Meanwhile, we expect headline PCE inflation to print at 0.4% m/m (0.35% unrounded), and for the y/y rate to remain at 2.4%.

A little better picture than January

The February inflation data were not great, but they were modestly encouraging after alarming data in January. Core PCE inflation should soften in February, but 0.28% m/m is still too high for the Fed. We continue to expect the Fed will start its cutting cycle in June with a 25bp cut. However, it will need to see more improvement in the upcoming inflation data to have enough confidence to begin to ease.

(Exhibits on next page)

Click US Watch for full report including important disclosures.

S&P 500 EPS Outlook

Entering a virtuous cycle – raising S&P 500 EPS

12 March 2024

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Raising 2024 EPS to $250, launching 2025 at $275

We raise our 2024 S&P 500 EPS estimate to $250 (+12% YoY; vs. $235 previously), the highest top-down forecast on the Street. Companies delivered another strong beat in 4Q (see 4Q earnings) and our economists raised their 2024 GDP forecast to +2.7% YoY (vs. +1.4% in November). The 1.3ppt increase in GDP forecast translates to a 5ppt boost to EPS growth, all else equal. 2023 was a transition year for Corporate America, and companies have now adjusted to the new higher rate and tepid demand environment. Our top-down framework suggests EPS undergrew by 3ppt in 2023, which should be recouped in 2024. We also launch our 2025 EPS forecast at $275 (+10% YoY). See our S&P EPS model.

AI's virtuous investment cycle

Hyperscalers (MSFT (Microsoft), AMZN (Amazon), GOOGL (Alphabet), META) are expected to spend $180B on capex in 2024E, +27% YoY (Exhibit 17). The $38B YoY increase in capex of represents ~80% of their expected earnings growth YoY – i.e., they're entering a reinvestment cycle. History suggests companies in reinvestment cycles underperform (Exhibit 20), but we see a potential virtuous cycle forming from AI (artificial intelligence) investments. Semis and networking are the most obvious beneficiaries (Exhibit 19), but increased power usage and the physical build-out of data centers will lead to more demand for electrification, utilities, commodities, etc. (see AI impact to Industrials, Utilities, Data Center REITs). Productivity gains from AI and domestic investments are also a major tailwind (Exhibit 26).

New economy is investing, old economy is cutting back

Excluding the hyperscalers, S&P 500 capex is expected to grow at just 1% YoY. This is the opposite of last year's trend when hyperscalers cut back 7% on capex, while the others increased capex by 9% YoY. Similarly, whereas Tech layoffs peaked last year, layoffs remain elevated in other sectors (Exhibit 14). As Big Tech enters an investment cycle and the old economy cuts costs/capex, we expect to see the growth differentials merge between Tech and the others (see Exhibit 34).

EPS cycle is different from the economic cycle

Goods/manufacturing represent 50% of earnings but just 20% of the economy (Exhibit 7). Hence, the post-COVID shift from goods to services resulted in an EPS recession despite above-trend GDP in 2023 (Exhibit 8). But we see continued signs of a manufacturing upcycle, signaling an end to the third-longest manufacturing downturn in history (Exhibit 9). Inventory levels are now just back to normal (Exhibit 10) and a re-stocking cycle could be next (see Truckers). Historically, when the ISM manufacturing PMI has been in expansion, S&P 500 EPS have grown 12% on average.

Risks: weaker demand & potential tariffs

Demand recovery will be the key driver of earnings in 2024-25. Although margins recovered from the lows on lower costs, further margin gains will need better demand. Potential tariffs in the event of a Trump victory in the presidential election are another key risk – e.g., assuming no price pass-throughs, we estimate a 5% EPS hit from 60% tariffs on Chinese imports, all else equal.

Click S&P 500 EPS Outlook for full report including important disclosures.

Exhibit 1: 2024-25 EPS forecast
BofA vs. consensus EPS forecast

	Btm-up analysts	YoY	BofA Strategy	YoY
1Q23	53.08	-3%	53.08	-3%
2Q23	54.29	-6%	54.29	-6%
3Q23	58.41	4%	58.41	4%
4Q23E	57.24	8%	57.24	8%
2023E	**$222**	**2%**	**$222**	**2%**
1Q24E	55.17	4%	57.00	7%
2Q24E	59.32	9%	61.00	12%
3Q24E	63.59	9%	65.00	11%
4Q24E	65.27	14%	67.00	17%
2024E	**$243**	**10%**	**$250**	**13%**
2025E	**$276**	**13%**	**$275**	**10%**

Source: FactSet, BofA Equity & Quant Strategy
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Exhibit 2: BofA Strategy 2024 EPS vs. top-down consensus
BofA vs. top-down6 strategists

BofA	**$250**
Top-down avg.	$235
Median	$235
High	$250
Low	$220
Sample size	21

Source: Bloomberg
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US Watch

Downward revisions tarnish a decent retail sales report

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February retail sales were tepid

Retail sales for February came in below consensus but firmer than our forecasts. Headline retail sales were up 0.6% m/m, supported by the surge in auto sales last month. The ex-autos component rose by 0.3% (consensus: +0.5%, BofA forecast: -0.1%). The core control group was flat (consensus: +0.4%, BofA: -0.3%).

Revisions stole the show once again

For the second consecutive month, there were large downward revisions to the prior two months' retail spending data. Ex-auto retail sales were revised down more than 0.5pp over December and January, while core control sales were marked down by more than 0.2pp on net. Therefore, the trajectory of retail spending looks significantly softer than it did when the data for December were released. For example, as of the latest data, ex-auto retail sales for December are 0.7pp weaker than they were in the initial release (Exhibit 2).

The details of the report were a mixed bag

Among the categories of retail sales, building supplies, autos, gas stations, and electronics & appliances saw large gains. The first three of these categories are omitted from the core control group, which is why it was weaker than the other aggregates. The pickup in gas spending was likely related to higher gas prices and payback for the weather disruptions in January. Recent gains in electronics & appliances appear to be payback for a massive drop in November. Meanwhile, furniture spending was particularly weak. Clothing, auto parts and health & personal care were also soft (Exhibit 1).

Restaurants and online shopping still the biggest drivers

Stepping back, restaurants & bars and nonstore retailers remain the most important drivers of retail spending over the last six months. The strength in spending at restaurants and bars is partially due to elevated inflation in food services, although inflation-adjusted spending has also held up well.

Demand is not re-accelerating

Similar to most of the other major data releases for February, the retail sales report suggests that the economy is not overheating. If anything, spending appears to have softened a bit. It remains to be seen how much of this is because of outright deflation in many goods categories, and how much of the slowdown in retail spending will be offset by robust services demand. Either way, the latest data flow should pare tail risks of re-acceleration.

Click US Watch. for full report including important disclosures.

Sector Focus Point

Consumer deep dive: a macro, quant and thematic perspective

Death of US consumer has been greatly exaggerated

We deconstruct large cap US consumer stocks (see SMID companion), where trends in consumption have slowed but defied expectations of collapse from rising borrowing costs and inflation. Why? Termed-out mortgages, tight labor markets and a nascent wealth transfer from cash-rich retirees to strapped Gen Y & Z helped. But real-time data point to a slowdown and a trade-down where higher income jobs have been cut, and AI could continue to disrupt. Overall, we still see more reasons to be bullish than bearish on the US consumer – we remain overweight Discretionary and underweight Staples.

Best stock-pickers' sector; doubly so post-COVID...

Consumer sectors have always had more idiosyncratic risk than others, where brand equity and product differentiation have resulted in lower correlations and higher dispersion across stocks. COVID's consumption impact – stockpiling, B&M to online, services bust to boom, supply chain issues, CPI/oil volatility, labor squeezes, helicopter money – doubled the idiosyncratic industry risk based on industry earnings correlations.

But 2024 is a big macro/policy year: elections, Fed

Globally and in the US, election risks loom large. Tax uncertainty could drive shifts in capex and consumption, or selling in big gainers (AMZN is a top retail holding based on GWIM data). Immigration/foreign relations policy shifts could affect labor and near-shoring trends, but China tariff impacts are mollified vs. 2018 given supply chain shifts since then. Easy monetary policy is correlated with consumer equity alpha, with four Fed cuts priced in for 2024. A shift in policy could impact stocks sensitive to short rates.

Secular shifts: productivity, automation, AI

Consumer companies are more labor intensive than any other sector and, like most US corporates over the last 20 years, shifted focus from efficiency-driven earnings to lower hanging fruit: global cost arbitrage and cheap capital. But margin risk from higher labor costs has been managed, and trends in automation show a renewed focus on efficiency, driving smoother earnings and multiple expansion – see inside for a case study.

A new aspirational consumer: India

According to Amish Shah, Head of India Strategy (Survey), shifts from staples to discretionary are in the works (grains to beverages, necessities to experiences). iPhone sales registered a remarkable 52% CAGR, with similar premiumization trends across big ticket (residence, autos) and low price point (laundry, beauty, biscuits). Per capita income should nearly double by FY30, making India the 3rd largest economy.

An empirical toolkit for consumer-focused investors

Positioning data indicate Discretionary being out of favor, which is one reason we are overweight. Also see metrics for picking consumer stocks, AMZN/TSLA impacts and more.

Click Sector Focus Point for full report including important disclosures.

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GFC: global financial crisis

B&M: brick and mortar

GWIM: Global Wealth & Investment Management

AMZN: Amazon.com

TSLA: Tesla

The RIC Report

Tax-efficient upgrades hiding in plain sight

The RIC Outlook

It was supposed to be “the year of the bond”. But Treasuries are on pace for a 13% loss, and with super-core inflation >4% & rising, are Fed cuts really that favorable for fixed income? We prefer quality equities, Prudent Yield credit, and scarce commodities.

The universal tax

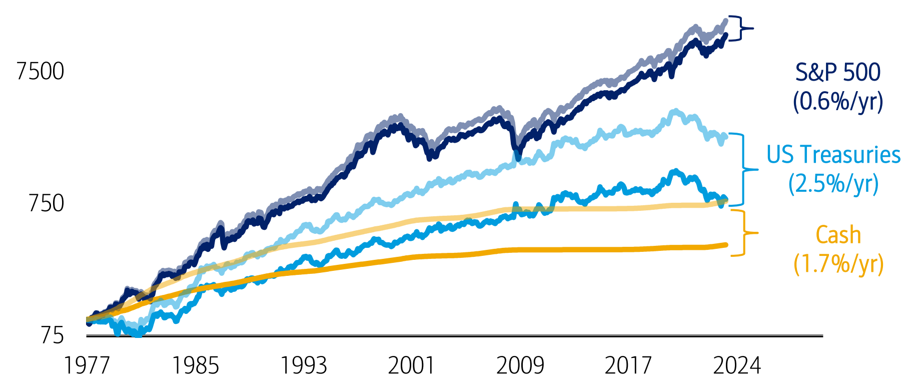
US federal debt will likely exceed 100% of GDP in July, soon surpassing the WWII peak. Almost 90% of the budget rises automatically. How does it end? Not with drama or default, but with taxes or with the hushed acceptance of that universal tax: inflation.

Five ways to make portfolios more tax-efficient

It’s March and Tax Day is coming. Ideas to start the conversation with a tax professional:

1. **Investment products**: the average exchange-traded fund (ETF) saves about 1ppt per year versus an identical mutual fund by avoiding taxable events.
2. **Asset allocation**: households bought $1tn of Treasuries & money markets in ’23. All those interest payments are taxable as ordinary income, e.g. at 37%. As the tax bill comes due, the 20% capital gains rate for equities is more attractive (Exhibit 1).
3. **Fixed income**: our Prudent Yield sectors offer 6% tax-adjusted yields vs just 3.5% for the US Aggregate Bond benchmark. High yield munis are key (see interview).
4. **Equities**: buybacks beat dividends by 4ppt/year through low-friction compounding.
5. **The rest**: ideas abound if you know where to look. We flag MLPs, QDI, & CEFs.

Exhibit 1: Taxes take 2-2.5ppt/year from bonds & cash; just 0.6ppt/year from stocks
Total return gross & net of taxes for different assets; # in parenthesis = annual tax drag



Source: BofA Research Investment Committee, Bloomberg, ICE Data Services, LLC. *We assume a 37% tax rate for US Treasuries & cash; 20% for S&P 500. Note: US Treasuries=G8O2; Cash=G0O1. See appendix for tax disclosures.

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Click The RIC Report for full report including important disclosures.

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View Transcript

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Any information relating to the tax status of financial instruments discussed herein is not intended to provide tax advice or to be used by anyone to provide tax advice. For more information see the appendix.

IT Hardware Industry

Artificial Intelligence set be a key driver for server market growth

Price Objective Change

13 March 2024

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Modeling double-digit CAGR for revs, high-single for units

In the 17-years from 2006 to 2023, the server market grew revenues at mid-single digit CAGR (5.4%), and units at low-single digit CAGR (2.8). We see Artificial Intelligence (AI) driving most of the future growth in server revenues over the next 4-years. We model the overall server market growing revenues double-digits (about 23% CAGR) between 2023-2027, while server units grow at high-single digits (8.6% CAGR) in the same timeframe. Within our coverage universe, we see Super Micro, DELL, and HPE directly benefiting from higher AI server demand, while NTAP, PSTG, WDC and STX benefit from increased demand for storage driven by increased AI workloads.

AI servers to grow much faster than the overall market

Figure 2 shows our estimate of AI versus non-AI server growth 2023-27. While we expect the overall server market to grow revenues at 23% CAGR, in that timeframe we expect AI server revenues to grow much faster at about 50% CAGR. Non-AI server revenues grow much slower at low-single digits (about 2.5% CAGR). We expect AI server units to grow at 58% CAGR 2023-27, while non-AI server units grow at mid-single digit CAGR (6.3%). This leads to total server market unit growth at 8.6% CAGR 2023-27. Within AI servers, we expect both Training servers and Inference servers to grow revenues double digits, with Training server revenues growing at about 36% CAGR 2023-27, while inference server revenues grow faster at about 66% CAGR.

Dell, Super Micro, HPE, Lenovo are the top server OEMs

In C4Q23 Dell, Super Micro, HPE, Lenovo and were the top server vendors by revenue. In terms of market share by revenues, Dell had 11.5% share, Super Micro 8.1%, HPE 6.9%, and Lenovo and IBM each with 4.0%. In terms of unit share, Dell had 11.7% share, HPE 6.7%, Super Micro 6.0%, Lenovo 4.8% and Cisco 1.2%.

Adjusting estimates and price objectives

We reiterate our Buy rating on Dell and adjust our revenue/EPS estimates. Our PO moves to $130 (from $116) on 15x (prior 14x) C25E EPS of $8.46 (prior $8.26). We apply a slightly higher multiple on expected higher revenue growth related to AI server demand. We reiterate our Neutral rating on HPE and our PO moves to $19 (from $17) on 8x C25E EPS of $2.26 (prior 9x C24E EPS of $1.94). We roll-over to a C25E based valuation. For NTAP, we reiterate our Underperform rating. Our PO moves to $85 (from $78) on 13x C25E EPS of $6.51. We roll-over to a C25E based valuation. For PSTG, we reiterate our Neutral rating. Our PO moves to $57 (from $50) on 5x (prior 4x) C25E EV/sales on better-than-expected revenue growth and profitability. For WDC, we reiterate our Buy rating. WDC recently positively pre-announced its F3Q24 quarter. We adjust our estimates, and our PO moves to $75 from $70 on 9x (unchanged) C25E EPS of $8.31 (prior $8.16). For STX, we reiterate our Buy rating. STX also recently pre-announced its F3Q24 quarter to the mid-point of prior guidance. We adjust our revenue and EPS estimates. Our PO moves to $110 from $100 on 13x (prior 12x) C25E EPS of $8.34 (prior $8.36). We use a higher multiple as growth and margins are rerating higher.

Ticker	Rating	PO (previous)	PO (revised)
DELL	BUY	$116	$130
HPE	NEUTRAL	$17	$19
NTAP	UNDERPERFORM	$78	$85
PSTG	NEUTRAL	$50	$57
WDC	BUY	$70	$75
STX	BUY	$100	$110

See inside for revenue and EPS estimate changes

AI: Artificial Intelligence
FCF: Free Cash Flow
n-t: near-term
l-t: long-term
PO: Price Objective

Investment decisions should not be made prior to reading the research report, which includes important information and disclosures.
Click IT Hardware Industry for full report including important disclosures.

US Consumer Staples

Takeaways from BofA Consumer & Retail Conference 2024

Industry Overview

14 March 2024

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Tickers mentioned

CCEP: Coca-Cola European Partners
CELH: Celsius Holdings
CPB: Campbell's Soup Co.
COCO: VitaCoco
HRL: Hormel Foods Corp.
KVUE: Kenvue
NAPA: Duckhorn Portfolio
PG: Procter & Gamble
PPC: Pilgrim's Pride
TAP: Molson Coors
TSN: Tyson Foods
UTZ: Utz Brands

12 Staples companies/meetings across two days in Miami

Earlier this week, we hosted our annual 2024 Consumer & Retail Conference for the second time in Miami, FL, where we hosted presentations and/or investor meetings with management teams from CPB, HRL, PPC, TSN, UTZ, CCEP, CELH, COCO, NAPA, TAP, KVUE, PG.

Food—SNAP roll-offs and summer to be key watch-outs

Snacking/center-store (CPB, UTZ) and protein (HRL, PPC, TSN) companies were in focus. Overall, volume trajectory continues to be a focal point with SNAP roll-off laps in March/April and the summer to be key watch-outs for potential positive inflection points. In snacks – snacking categories, particularly salty snacks, have seen sluggish scanner data as it was one of the last categories to feel elasticities. As we move closer into the summer (bigger snacking season) and promotional/merchandizing activity potentially unlocking incremental demand, snacking volumes could see some relief. We expect UTZ to be differentiated in this regard as a share gainer and upgraded to Buy this morning in a separate report. CPB also announced the closing of the SOVO acquisition on Tuesday morning. In protein – Chicken fundamentals continue to be strongest with some analogies that '24 could set up similar or close to '15-'17 profit cycle. Pork availability is improving after a liquidation period given improved herd health. Cattle cycle remains challenged as heifer retention remains elusive.

Beverages— Teeing up summer activations

CCEP, CELH, NAPA and COCO hosted meetings and TAP held a fireside chat. CCEP reiterated a bullish tone for 2H24, with strong summer activation around the Olympics and soccer lapping against easy comps. With the Philippines deal closed, management spoke to margin expansion potential over the long term from improved sugar costs. CELH highlighted their strong US growth runway driven by incremental fridge and shelf placements, with a willingness to invest behind growth vs blowing out gross margins this year. TAP sounded upbeat about US market share in 1Q, confident in the prospect of holding last year's gains. COCO confident in sales outlook this year, freight seems manageable, plenty of distribution runway, and new pack configurations. NAPA sees luxury wine category growth of 0-1% for rest of year but expects company-specific dynamics to outpace.

HPC— Innovation takes focus for PG and KVUE

PG and KVUE hosted investor meetings. In 2024, Kenvue has a strategy to improve in skin health & beauty, with: 1) increasing marketing, 2) increasing innovation, and 3) increasing in-store execution. Longer-term, to drive actionable change within the organization, Kenvue is aligning compensation incentives with driving profitable growth with margin expansion, rather than a primary focus of efficiency to maximize FCF. On innovation, Procter showed off its new Tide Evo laundry tile which is in test and should hit shelves later this year. By market, the US sounded strong, Latam is faring better thanks to catch-up pricing in Argentina, and China weakness is moderating but still a drag through FY24.

Investment decisions should not be made prior to reading the research report, which includes important information and disclosures.
Click US Consumer Staples for full report including important disclosures.

Restaurants Industry

Consumer Conference Takeaways: CMG, FWRG, JACK, PTLO, QSR, SG, TXRH

Price Objective Change

14 March 2024

Equity
United States
Restaurants

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CMG: Throughput, LTOs, loyalty

Throughput remains an opportunity: 50% of stores had 4 people on the front makeline at peak periods in 4Q - from 30% in 3Q - but well below 2014/15 (70%+). Service speed amplifies traffic drivers like LTOs (relaunch of Chicken al Pastor) and loyalty (suggestive selling, incentives to drive frequency). CMG will test robotics - Hyphen, Autocado - in store this year (see link to Restaurants Technology: Automating restaurants).

PTLO: Strong value prop, portable concept

The Sunbelt will account for 80% of PTLO's unit growth with AZ, TX, and FL underpinning a 3 yr AUV of $7.3-7.45mm (present sunbelt avg of $6.8mm includes stores predating the current RE strategy). PTLO's prices compare favorably to other fast casuals (~$13 avg check vs ~15-$17) and PTLO is leaning in to menu news (salads).

SG: QTD demand strong; IK benefits bottom and top line

Ex-weather and calendar shifts, 4Q momentum carried into 1Q (seeing LDD comps) and traffic continues to benefit from throughput, innovation, and healthier new markets. Infinite Kitchen drives labor savings (700 bps to margin) with potential added benefits to topline (throughput). We raise our PO from $21 to $24 on a higher terminal multiple (26x vs 22x prior) in line with mature growth restaurant peers as market multiples have expanded.

JACK: Smashed Jack supports comp; unit growth to accel

JACK's softer start to C24 reflects weather and competition, but also a gap in marketing as the Smashed Jack launch was delayed to ensure sufficient supply (without ads, it mixed MSD, the same as prior ad-supported launches). AUVs in white space (Salt Lake) remain high; expect growth from new devt commitments to ramp (16 mos build time).

QSR: Ops, remodels in US, NRG in int'l

As QSR aims to reaccelerate unit growth (of 5% LT vs 3.9% in F23 and ~4.5% in F24E), its focus is on encouraging China licensees to ramp (but not funding growth for BK China and Tim Horton's China). In the US QSR expects to spend $300mm to support franchisee remodels but is focused on ops rather than deep discounts to drive sales NT.

FWRG: Culinary, value drive growth in competitive mkts

While FWRG's 1Q started soft, the absence of check management suggests no change to consumer spending trends. Innovation (5 LTOs per year) remains a key traffic driver while tech (pay at table) is helping serve unmet demand. Market research, unit economics support growth even in competitive markets like Las Vegas and New England.

TXRH: LT traffic share gains, op leverage emerging

TXRH relies heavily on managers in the markets to help determine market-appropriate pricing; despite CDR promos, traffic continues to gap out. As TXRH again leverages labor (labor hours growth <50% traffic growth) and favorable commodities we see earnings upside. TXRH reiterated its 900 store target, but small market success suggests to us that could tick higher.

Investment decisions should not be made prior to reading the research report, which includes important information and disclosures.
Click Restaurants Industry for full report including important disclosures.

Stock symbol key:
CMG: Chipotle
PTLO: Portillo's
SG: Sweetgreen
JACK: Jack in the Box
QSR: Restaurant Brands Int'l
FWRG: First Watch
TXRH: Texas Roadhouse

Glossary of terms:
LDD – low double digit

MSD- mid-single digit

AUV- average unit volume

CDR- casual dining restaurant

LT- long term

NT- near term

LTO- limited time offer

RE- real estate

IK- infinite kitchen

Walmart Inc

Consumer Conference Key Takeaways

Maintain Rating: BUY | PO: 67.00 USD | Price: 61.41 USD

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Key highlights from WMT group meetings

We hosted WMT Investor Relations for group meetings at our 2024 Consumer Conference in Miami, FL. We reaffirm our Buy rating and highlight key takeaways below:

WMT is gaining unit share across categories

WMT continues to gain share in both grocery & general merchandise, with overall unit sales positive for WMT in F4Q in contrast to cont'd negative (but improving) trends for the industry. WMT is seeing unit growth across categories excl. certain areas of general merchandise with longer life cycles (vs. positive units in higher velocity areas like apparel & home). In both 3Q & 4Q, WMT grew share across all 9 categories of general merch.

Dry grocery disinflation has slowed, WMT is pushing back

While general merchandise deflation continues (tracking in the -HSD-LDD% range), and WMT's private label brand portfolio is also deflationary overall, WMT continues to see inflation in dry grocery and consumables on the national-branded side (which had been slowing until F4Q). Now as disinflation has slowed, WMT is working diligently with its suppliers to help push back on prices (incl. encouraging the renegotiation of rates from manufacturers where it makes sense).

WMT continues to work towards 1P ecom profitability

WMT remains focused on improving ecommerce profitability and sees a path to 1P ecom breaking even in the next ~3 years when including subsidization streams (digital advertising, memberships etc.). In the next ~5 years, WMT could achieve 1P ecom profitability on a standalone basis by densifying routes (helped by WMT's Spark Driver platform, which not only fulfills the vast majority of last mile delivery for WMT but is also open to other retailers) and growing general merchandise mix.

See support from growing digital advertising revenue

We see margin support for WMT as increasing contributions from higher-margin profit streams (including digital advertising, 3P marketplace & fulfillment services) help offset ongoing mix headwinds (as sales of higher-margin general merchandise likely continue lagging grocery & health/wellness). In addition to WMT's existing digital advertising business ($3.4bn at F24 year-end), WMT now has meaningful potential in the connected TV advertising space supported by its recently announced acquisition of VIZIO.

Automation enabling labor productivity

WMT continues to add labor hours to its store network given continued ecom growth & the utility of stores to fill orders. However, WMT should be able to grow its business without meaningfully expanding its workforce as it unlocks profitability through tech & automation. By automating some of its most hour-intensive and least enjoyable tasks (such as shelf price changes), WMT is able open up time for associates to help customers. I.e., Sam's Club last year eliminated 35mn tasks from its associate experience and redeployed those hours to its growing curbside pickup business.

Investment decisions should not be made prior to reading the research report, which includes the opinion key and other important information and disclosures.
Click Walmart Inc for full report including important disclosures.

Stock Data

Price	61.41 USD
Price Objective	67.00 USD
Date Established	20-Feb-2024
Investment Opinion	A-1-7
52-Week Range	45.53 USD - 61.57 USD
Mrkt Val (mn) / Shares Out (mn)	593,589 USD / 9,666.0
Free Float	53.3%
Average Daily Value (mn)	1418.22 USD
BofA Ticker / Exchange	WMT / NYS
Bloomberg / Reuters	WMT US / WMT.N
ROE (2025E)	19.5%
Net Dbt to Eqty (Jan-2024A)	34.7%
ESGMeter™	Medium

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Key terms:

HSD = high single-digit

LDD = low double-digit

1P = first party

3P = third party

TopBuild Corp

TopBuild: incrementally bullish following management meetings

Reiterate Rating: BUY | PO: 475.00 USD | Price: 411.50 USD

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Equity

Key Changes

(US$)	Previous	Current
Price Obj.	410.00	475.00

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Incrementally bullish following management meetings

We hosted investor meetings with TopBuild CFO Rob Kuhns and Investor Relations PI Aquino. We came away incrementally bullish: 1) guidance is conservative relative to our expectations on single-family starts and insulation pricing, 2) BLD still has opportunity to drive elevated incremental margins from productivity initiatives, and 3) increased penetration of spray foam could drive relative outperformance vs industry at a high profit dollar contribution. We raise our PO to $475 (from $410) based on ~13X EV/2025E EBITDA (previously ~11X EV/2025E EBITDA) driven by higher sector multiples and an improved single-family/pricing outlook. Reiterate Buy. See our key takeaways below:

Single-family momentum improved into February

TopBuild had a slow start to 2024 due to adverse weather in January, but trends improved in February. TopBuild's guidance conservatively assumes single-family starts roughly in-line with the current trend (low-to-mid single% YoY in 2024) but we see upside to the starts outlook and expect single-family starts to increase ~9%. Builders (both public and private) appear optimistic on the starts pace in 2024 (and into 2025). TopBuild's multi-family (estimate mid-teens % of residential and 10% of total) backlog carries through 2024.

Plenty of offsets to office softness in non-residential

Urban office and warehouse end markets are soft, but this should be more than offset by data centers, semi-conductor plants (Chips ACT), EV battery plants and LNG refiners. BLD is already bidding out to 2025 for some projects. Commercial pricing increased slightly in 1Q24 and mineral wool capacity is tight.

We see upside to fiberglass pricing outlook

Fiberglass insulation capacity is already tight (expect flattish industry capacity overall in 2024 with 3% growth from Knauf Texas facility opening offset by maintenance downtime). The mid-point of guidance implies realization of the already announced 1Q pricing (we interpret as low-single digit) and additional hikes would be upside. Given the tight capacity and increased pace of single-family starts, we anticipate an additional price increase from manufacturers later in 2024.

Margins could benefit from productivity improvements

BLD has been driving incremental margins above its long-term target of 22-27% due to productivity gains, acquisition synergies and favorable price-cost. We see potential upside to the 2024 guidance of 22-27% (excluding $25mm in benefit of multi-family shipments in 2023) on additional productivity gains and pricing. There is still a wide spread between BLD's most and least productive branches, which leaves plenty of efficiency headroom.

See below for outlook on spray foam, M&A and SPI.

Stock Data

Price	411.50 USD
Price Objective	475.00 USD
Date Established	14-Mar-2024
Investment Opinion	B-1-9
52-Week Range	184.50 USD - 421.75 USD
Mrkt Val (mn) / Shares Out (mn)	13,076 USD / 31.8
Free Float	99.3%
Average Daily Value (mn)	102.50 USD
BofA Ticker / Exchange	BLD / NYS
Bloomberg / Reuters	BLD US / BLD.N
ROE (2023E)	27.9%
Net Dbt to Eqty (Dec-2022A)	63.1%
ESGMeter™	Medium

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SPI- Specialty Products & Insulation

BLD – TopBuild

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Evergy, Inc

Kansas-style PISA? We'll take a slice. Upgrade to Buy on lag improvement

Rating Change: BUY | PO: 57.00 USD | Price: 51.27 USD

Risk/reward attractive with accumulating interim recovery

We upgrade shares of Kansas- and Missouri-based electric utility Evergy (EVRG) from Neutral to Buy due to the improving regulatory/legislative backdrop. The draft Kansas Legislature House Bill 2527 (HB2527) including Plant in Service Accounting (PISA) mechanism proposed is doubly supportive for Evergy. **The bill passed the House yesterday March 12th**. As amended, the bill would reduce regulatory lag supporting higher earned ROEs and provide for EPS growth stability & visibility. Separately, Missouri has its own draft legislation (HB2541/SB1422) that would expand and extend PISA, further de-risking shares. We forecast 6%+ 2023-2028 EPS growth.

Stakeholders are more supportive of EVRG recently

Throughout the HB2527 process, our local Kansas stakeholder conversations have been more constructive than in years past. EVRG has had to overcome a wide range of regulatory challenges in both Kansas and Missouri but has finally recalibrated its outlook and made progress with influential intervenors in both states from our discussions. While it could take time for this to prove-out, we believe that the ongoing Missouri rate case and next Kansas rate cases will be less controversial. Per the Kansas legislature, the bill will allow EVRG to build more dispatchable resources like natural gas for reliability.

EPS growth rate looks closer to 6%, supporting avg P/E

We estimate that PISA would improve EPS approximately $0.10 annual run-rate upon implementation and ~$0.15 later in the plan. The combination of PISA and a moderation of long-term interest rates supports a 6-6.5% EPS CAGR, above the newly lowered 4-6% 2023-2026 CAGR. We do not expect management to change its long-term EPS or capital expenditures guidance in the near-term but this provides more confidence that EVRG can grow closer to its peers at 5-7%. In the long-term, the combination of economic development rate schedules and more streamlined regulation could lead to more robust rate base growth than the below-average 5.7% 2023-2028 currently projected.

Valuation is modest and has a favorable risk/reward

EVRG currently trades at a ~12% discount vs peers, one of the largest for utilities, despite what we see to be an average growth rate, reasonable balance sheet, and a rate-of-change story after legacy regulatory issues. We increase the PO from $51 to $57 primarily from +$4/sh mark-to-market and +$4/sh lowering to -1x P/E discount from -2x previously and ~-$1/sh reflecting -1% moderation in 2026 EPS.

Estimates (Dec) (US$)	2022A	2023A	2024E	2025E	2026E
EPS	3.71	3.54	3.80	4.05	4.21
EPS Change (YoY)	4.8%	-4.6%	7.3%	6.6%	4.0%
Consensus EPS (Bloomberg)			3.83	4.01	4.23
DPS	2.33	2.48	2.60	2.72	2.85
Valuation (Dec)					
P/E	13.9x	14.6x	13.6x	12.7x	12.3x
Dividend Yield	4.5%	4.8%	5.0%	5.3%	5.5%
EV / EBITDA*	13.6x	12.7x	11.9x	11.4x	10.9x
Free Cash Flow Yield*	-3.1%	-4.8%	-4.0%	0%	-2.3%

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Equity

Key Changes

(US$)	Previous	Current
Inv. Opinion	B-2-7	B-1-7
Inv. Rating	NEUTRAL	BUY
Price Obj.	51.00	57.00
2024E Rev (m)	5,962.6	5,869.0
2025E Rev (m)	6,129.8	6,048.2
2026E Rev (m)	6,348.9	6,215.3
2024E EPS	3.82	3.80
2025E EPS	4.04	4.05
2026E EPS	4.27	4.21
2024E DPS	2.67	2.60

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Stock Data

Price	51.27 USD
Price Objective	57.00 USD
Date Established	13-Mar-2024
Investment Opinion	B-1-7
52-Week Range	46.92 USD - 63.93 USD
Mrkt Val (mn) / Shares Out (mn)	11,818 USD / 230.5
Free Float	98.5%
Average Daily Value (mn)	148.85 USD
BofA Ticker / Exchange	EVRG / NYS
Bloomberg / Reuters	EVRG US / EVRG.OQ
ROE (2024E)	8.9%
Net Dbt to Eqty (Dec-2023A)	131.9%
ESGMeter™	High

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HB: House Bill | SB: Senate Bill
PISA: Plant in Service Accounting

Price objective basis & risk

Chipotle Mexican Grill (CMG)

Our $3,000 price objective is based on earnings power. At the current unit growth rate, we think Chipotle should be able to reach its targeted 8000 store count in roughly 7 years. By then we'd expect AUVs to exceed $4mm - under the assumption that comps increase in-line with cost inflation - and margins to be in line with prior peaks of 27%. Assuming a G&A of 5%, which is more similar to mature company operated systems, this system would generate $7.9bb in EBITDA. At a 20x multiple, consistent with current valuation multiples on high growth companies, the implied EV would be $173bb, or $77bb discounted back to today. We then add the current net cash and project out 12 months to derive our price objective of $3,000.

Downside risks are: 1) lower than expected consumer uptake of new product innovations or digital ordering capabilities, 2) higher than expected food or labor costs that Chipotle is unable to offset with increased pricing, and 3) macroeconomic pressures that slow consumer income growth or otherwise dampen consumption.

Dell Technologies Inc. (DELL)

Our PO of $130 is based on approximately 15x our C25 EPS estimate of $8.47. Our target multiple compares to median 5x of historical range 3x-8x for Dell since it returned to the public markets in 2019. Dell went private in 2013 and prior to that the company had a very different structure. As such, we do not believe earlier historical trading multiples are meaningful. In our opinion, a multiple higher than the historical range is warranted given improved storage portfolio, lower financial leverage and it balances opportunities to invest in core areas of growth, with ongoing weak macro and component shortages.

Downside risks: faster-than-expected slowdown in the global economy, which could prove to be a headwind to revenue growth, faster-than-expected strengthening of the U.S. dollar, trade war with China, and higher-than-expected tariffs, Dell not being able to source needed processors from Intel, new sales teams not being able to ramp as expected, and unexpected share loss to competitors.

Upside risks: faster-than-expected revenue growth and market share gain, faster mix shift to storage and premium PC and server configurations, which can drive upside to margins, faster-than-expected ramp of new sales teams, and component shortages normalizing more quickly than expected, which can drive upside to cash flow.

Evergy, Inc (EVRG)

Our $57 price objective for Evergy (EVRG) is based on sum of the parts valuation, applying an in-line utility peer 2026E P/E of 13.9x. The electric peer P/E multiple is grossed up for one year by 5% to reflect capital appreciation across the sector. We further apply a -1.0x turn discount across Missouri and -1x for the Kansas Central subsidiaries based on our perception of a challenging regulatory setup that will pressure future capital spend and Evergy's ability to sustain a consistent EPS growth rate in light of intense regulator scrutiny of customer bill pressures.

Downside risks to our price objective are adverse regulatory outcomes, inability to deploy capital expenditures consistent with guidance, operational performance issues including at the nuclear facility, and earning below the authorized rate of return. Upside risks to our price objective are favorable regulatory outcomes in important proceedings, accretively deploying additional capital expenditures above guidance, higher than anticipated O&M benefits and merger synergies leading to a higher earned return on equity, and the ability to recover capital invested in retired coal assets

First Watch (FWRG)

We believe FWRG should trade a premium consistent with its faster growth and higher returns. FWRG currently trades in line with its peer group of restaurants and retailers with similar above-market growth rates. We believe a valuation in line with other high growth peers is justified owing to FWRG's faster than average topline growth, extended growth runway, as the brand goes national, and higher incremental returns, with restaurant level ROIs of about 40% or 2x other full service restaurants. We apply a 15x multiple to our forward EBITDA estimates (F25, $134mm) to arrive at our $31 PO. This target multiple is conservative relative to high growth peers' average of 17x.

Downside risks: higher-than-expected cannibalization of existing restaurants due to new store openings, staffing challenges and/or higher-than-expected wage inflation, higher-than-expected occupancy costs as First Watch ramps-up new stores at a faster rate. Upside risks: higher-than-expected AUVs of new units, faster-than-expected SSS growth, lower labor and G&A costs.

Hewlett-Packard Enterprise (HPE)

Our PO is $19 based on 8x our C25E EPS of $2.26. Our target multiple is just slightly lower than the median (9x) of the historical range (6x-13.0x). In our opinion, this multiple is justified as it balances positives including that HPE now has a better growth profile, and lower Tier-1 server sales and free cash flow is more in-line with normalized values, vs. near-term macro headwinds and risk from high backlog and slower customer acceptances.

Downside risks to our PO are larger than expected economic slowdown due to inflation and rising interest rates, on-going component availability concerns, COVID19 related shutdowns in China, more aggressive server pricing from competitor Dell, a faster than expected adoption of As-a-Service offerings which can pressure revenues in the near-term, unexpected share loss and slower than expected mix shift to higher margin products and services, FX headwinds, restructuring and execution challenges.

Upside risks are share gains, steady margin improvement and lower than expected restructuring costs and better free cash flow.

Jack in the Box (JACK)

Our $104 price objective is based on a 0.7x relative PE multiple (13.8x absolute) applied to our 12 month forward earnings estimates (2Q25-1Q26: $7.56). This is a material discount to highly franchised peers, given historically slower growth and more capital-intensive ownership model.

Downside risks to our price objective are: 1) sales could soften due to economic or competitive pressures, 2) food and labor costs rise and margins come under renewed pressure, 3) execution risk around speed of service, menu and marketing initiatives which are critical to driving sales at Jack in the Box.

NetApp Inc. (NTAP)

Our price objective (PO) of $85 is based on 13x C25E EPS of $6.51. This multiple is in the lower half of the historical range of 10-18x. We believe this multiple balances the benefit of potential revenue growth in All Flash Arrays against the long-term risk from data-center migration to the Cloud, and technological pressure from emerging competitors.

Upside risks are faster-than-expected growth in public cloud revenues and lower drag from investments, unexpected share gain from competitors, unanticipated large M&A, which drives revenue growth faster than expected, and faster-than-expected penetration of Flash into the existing NetApp installed base.

Downside risks are extended component shortage, an unexpected slowdown in the economy, higher-than-expected inflation, stall in the installed base refresh, material share loss in the Flash and Converged technology space, including Hyper Converged to competitors, acceleration of storage moving to the public cloud, and decline in penetration and success beyond the top enterprise accounts.

Portillo's Inc. (PTLO)

We set our $25 PO based on steady state earnings power. We assume PTLO grows its store base at 13% to reach 725 stores in the long term, and that average volumes grow with inflation. At $7.7 bb in sales, assuming stable RLMs and 8% G&A, PTLO would generate $1.4 bb in EBITDA. Applying an 11x multiple and discounting back equates to a $25 fair value in one year.

Risks to our PO: potential industry headwinds from wage inflation (MSD-HSD run rate for the industry) and food cost volatility, inability to fully offset downward pressure on volumes and margins from new store openings, and execution risks as the company looks to sustain a 10% unit growth rate.

Pure Storage (PSTG)

Our PO of $57 is based on 5x C2025E EV/Sales. This multiple compares to median 3x of historical range 1x-5x. Given Pure's strong revenue growth relative to other storage peers, we view 5x as appropriate (premium based on faster growth relative to peers).

Upside risks to our PO are faster recovery in the commercial segment, lower flash costs, sooner than expected recovery in the supply chain, and unexpected share gains.

Downside risks to our PO are an extended economic slowdown, rising costs, competition from well-established vendors like NetApp, Dell-EMC and HP that control vast distribution networks and have the ability to deeply discount products for certain customers, competition from private companies, enterprise movement to the public cloud, execution-related issues due to the high-growth nature of the company, and erosion of its competitive advantage in operating software over time.

Restaurant Brands International Inc. (QSR / YQSR)

We view QSR's 5-yr historical average multiple of 1.1x as appropriate as lagging sales trends and greater investment needs drive lower estimate revisions. We apply this multiple to our 12 months forward EPS estimate (F25) EPS to arrive at a price objective of $78 (C$105.83). Our 1.1x relative multiple (vs the S&P 500) translates to an absolute P/E multiple of 20.9x.

Upside risks: better-than-expected results on sales trends and market share gains as a result of investments in stores, technology, and marketing spend. Faster-than-expected turnaround in the Burger King brand. Faster-than-expected growth of the Tim Horton's brand.

Downside risks: Higher-than-expected G&A spending, continued lag in topline growth trends relative to competitors, slower-than-expected recovery in supply chain and/or labor constraints associated with COVID-19.

Seagate Technology (STX)

Our PO of $110 is based on 13x our C2025E EPS estimate of $8.34. This multiple is towards the higher end of the historical P/E range of 7x-13x, and is warranted in our view as earnings momentum turns positive and peak earnings can be higher than historical peaks. Earnings are at a cyclically historic low and hence we look out to C25 for a more normalized earnings power of the company. The multiple balances near-term headwinds against the return of a more rational HDD industry and back to revenue and EPS growth.

Downside risks to our price objective are: (1) further unit declines in desktops and notebooks, (2) worse than expected industry pricing, (3) increased usage of NAND flash, (4) share loss to WDC in the enterprise HDD market, and (5) degradation of cash position and potential violation of credit facility covenants. Upside risks are: (1) significant pickup in high capacity/nearline HDDs, which could drive ASPs and gross margin higher, (2) improved technological advantage over NAND flash so as to reduce SSD penetration, (3) consumer PC refresh cycle, and (4) improved free cash flow generation.

Sweetgreen (SG)
Our $24 PO is based on normalized earnings power. Assuming SG is able to reach its long-term target of 1000 stores in ten years, with 18% restaurant-level margin and 8% G&A, we arrive at $274mm EBITDA. We apply a 26x terminal multiple - consistent with mature growth restaurant peers after adjusting for SG's domestic, company-operated status - to arrive at EV of $7.1 bb, discounted back to today at 13%.

Downside risks are i) slower SSSG as a result of lower discretionary spending, ii) inability to gain traction in new markets outside of the urban core, iii) failure to offset food and labor cost inflation through pricing and volume growth, iv) worse than expected development challenges (construction costs, permitting) which could limit unit growth.

Texas Roadhouse (TXRH)
We view TXRH's 5-year average of 1.3x (excluding COVID spike) as the appropriate target multiple given TXRH's best-in-class traffic trends and topline growth and our expectations for further operating leverage. Our PO of $160 is based on a relative multiple of 1.3x (vs the S&P 500 index, or a 24.4x absolute multiple) on our 12-month forward EPS (F25, $6.54).

Downside risks are: i) lower-than-expected retail beef prices and as a result, decreased value proposition for steakhouses, ii) traffic growth deceleration in response to menu price increases, iii) greater than expected slowdown in consumer spending / macroeconomic risk pressuring discretionary income, iv) slower than expected unit growth at Texas Roadhouse.

TopBuild Corp (BLD)
Our $475 price objective (PO) is based on a 13x EV/2025E EBITDA multiple,above its average from 2017-2023 due a stronger growth outlook and improved margin profile.

Upside risks to our PO: 1) faster-than-expected recovery in new home starts, 2) further residential market share gains through organic growth and M&A, 3) continued strength in the commercial/industrial market, 4) continued price increases on insulation products.

Downside risks: 1) a downturn in the housing market leading to less starts, 2) deflation in insulation products leading to weaker revenue growth and margin pressure, 3) a broad pullback in commercial/industrial activity.

Utz Brands (UTZ)
Our $22 PO is based on 18.0x CY25 EV/EBITDA estimate. At this multiple, we value shares of UTZ at a premium to "platform companies" and companies that compete in the salty snack category given what we believe is an embedded take-out premium. Our target multiple of 18.0x is in line with past snack transactions - Hostess (17.2x X synergies), Dot's Pretzels (17.3x) and Snyder's-Lane (19.9x).

Upside risks are 1) faster category/brand growth vs peers and market share gains, 2) better-than-modeled cost synergies and 3) deflationary cost basket

Downside risks are 1) bigger-than-expected volume hit from price increases, 2) geographic expansion faces challenges, 3) cost synergies do not achieve targets

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Walmart Inc (WMT)

Our $67 price objective is based on 27x our F26E adj. EPS of $2.50, which is above WMT's average 2-year forward P/E multiple of roughly 21x but in line with a high of 27x over the past 5 years. Our multiple reflects an outlook for positive US comps (with positive traffic), omni-channel momentum, and healthy free cash generation. This P/E is more in line with other high-performing retailers but still a discount to other global ecommerce retailers.

Downside risks to our PO are the impacts of FX, pharmacy headwinds, slowing food inflation or deflation, Walmart's longer-term ability to continue gaining incremental market share given its large size, a weakening global retailing environment, competitive pressures at Sam's Club and/or Walmart International.

Western Digital Corporation (WDC)

Our PO of $75 is based on 9x C25E EPS of $8.31. This multiple is inline with 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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Important Disclosures

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R1]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R1]Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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